BANK LEUMI LE-ISRAEL B.M. AND ITS INVESTEE COMPANIES

Annual Report 2013

Bank Leumi le-Israel B.M. Head Office: 34 Yehuda Halevi Street, Tel Aviv 65546, Israel

The Bank has received the consent of the Supervisor of Banks to the publication of the annual financial report on a consolidated basis only, with condensed statements of the Bank (not consolidated) in note 29 to the financial statements.
The figures of the Bank alone are available on request from the offices of the Bank at 34 Yehuda Halevi Street, Tel Aviv or on its website: www.bankleumi.com.
This is a translation from the Hebrew and has been prepared for convenience only. In the case of any discrepancy, the Hebrew will prevail.

Bank Leumi le-Israel B.M. and its Investee Companies
Annual Report 2013

Index

David Brodet, Chairman[(1)]

David Avner

Rami Avraham Guzman

Prof. Arieh Gans

Moshe Dovrat[(2)]

Shai Shachnai Hermesh[(3)]

Adv. Miriyam (Miri) Katz

Yoav Nardi[(2)]

Adv. Haim Samet[(5)]

Nurit Segal[(3)]

Zipporah Samet

Amos Sapir

Prof. Efraim Sadka

Professor Yedidya Zvi Stern

Prof. Gabriela Shalev[(4)]

(1) Re-elected as director at the Annual General Meeting of the Bank held on 23 October 2013. On 9 January 2014, and after receiving the approval of the Bank of Israel on 5 January 2014, the Board of Directors of the Bank approved the term of office of Mr. David Brodet as Chairman of the Board of Directors, until the next General Meeting, at which the Chairman of the Board of Directors will stand for election as a director for a period of three years.

(2) Re-elected at the Annual General Meeting of the Bank held on 23 October 2013.

(3) Elected as directors at the Annual General Meeting held on 23 October 2013. Their term of office came into force on 5 January 2014.

On 31 March 2013, Mr. Doron Cohen resigned from his position as Director in the Bank.
In addition, on August 31, 2013, Mr. Yehuda Drori resigned from his position as Director in the Bank.

(4) Re-elected as external director pursuant to sections 239 and 245 of the Companies Law, 1999, at the Annual General Meeting held on 23 October 2013 for a period of three years from 1 February 2014.

(5) The appointment of Mr. Haim Samet as an external director pursuant to section 239 of the Companies Law was ratified at the Annual General Meeting held on 23 October 2013.

Bank Leumi le-Israel B.M.
Members of Management and their Positions*

Rakefet Russak-Aminoach, C.P.A. (Isr.)
President and Chief Executive Officer

Prof. Daniel Tsiddon(1)
Deputy Chief Executive Officer, Head of Capital Markets, Private Banking and Strategy Division

Yaacov (Kobi) Haber(2) (4)
First Executive Vice President, Head of Corporate and Commercial Division

Dan Cohen
First Executive Vice President, Head of Human Resources Division

Itai Ben-Zeev(3)
Executive Vice-President, Head of Capital Markets Division

Dr. Hedva Ber
Executive Vice President, Chief Risk Officer, Head of Risk Management Division

Adv. Nomi Sandhaus
Executive Vice President, Chief Legal Advisor, Head of Legal Division, Legal Risks Manager

Ms. Tamar Yassur
Executive Vice President, Head of Banking Division

Mr. Dan Yerushalmi
Executive Vice President, Head of Operations and Information Systems Division

Mr. Yoel Mintz(4)
Executive Vice President, Head of International Credit and Real Estate Division

Mr. Ron Fainaro C.P.A. (Isr.)(5)
Executive Vice President, Head of Economics and Finance Division

Shlomo Goldfarb, C.P.A. (Isr.)(5)
Executive Vice President, Chief Accounting Officer, Head of Accounting Division

---

Sasson Mordecai
Executive Vice President, Chief Internal Auditor, Head of Internal Audit Division

Adv. Yael (Ben Moshe) Rudnicki
Bank and Group Secretary

Somekh Chaikin, Kost Forer Gabbay & Kasierer
Joint Auditors of the Bank

(1) From 1 April 1 2013, Professor Daniel Tsiddon serves as Deputy Chief Executive Officer, Head of Capital Markets, Private Banking and Strategy Division. Until 31 March 2013, Professor Daniel Tsiddon served as Deputy Chief Executive Officer, Head of Capital Markets Division.
(2) On 1 January 2014, the Corporate Division and the Commercial Division were consolidated into one division – the Corporate and Commercial Division, headed by Mr. Yaacov (Kobi) Haber. With effect from 1 January 2013 until 31 December 2013, Mr. Yaacov (Kobi) Haber served as Head of Corporate Division. Until 31 December 2013, Mr. Gidon Altman served as Head of Commercial Division.
(3) With effect from 1 April 2013, Mr. Itai Ben-Zeev serves as Head of Capital Markets Division, subject to the Capital Markets, Private Banking and Strategy Division.
(4) With effect from 1 January 2014, Mr. Yoel Mintz serves as Head of International Credit and Real Estate Division, subject to the President and Chief Executive Officer. This division is also responsible for the Special Loans Unit. Until 31 December 2013, Mr. Yoel Mintz served as Head of the Structured Finance and Real Estate Division, subject to the Head of the Corporate Division.
(5) With effect from 1 April 2013, Mr. Shlomo Goldfarb serves as Chief Accounting Officer and Head of Accounting Division, subject to the Head of the Economic and Finance Division. Until 31 March 2013, Mr. Menachem Schwartz served as Chief Accounting Officer and Head of the Accounting Division. Mr. Menachem Schwartz retired from the Bank on 31 October 2013.

* Further details on the Bank management are presented in the Periodic Report of the Bank for 2013 and on the Magna website of the Israel Securities Authority http://www.magna.isa.gov.il

Bank Leumi le-Israel B.M. and Its Investee Companies

Directors' Report

The following is the sixty-third annual report of Bank Leumi le-Israel B.M. and the one hundred and twelfth report of the business, founded in 1902. This report will be presented to the Bank's Annual General Meeting. This report is based on an analysis of the data included in the Bank's Financial Statements and Management Review, and on additional data as required. This report is prepared in accordance with the public reporting directives of the Supervisor of Banks.

B. General Developments in the Group's Business

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

Bank Leumi and its subsidiary companies constitute one of the largest banking groups in Israel, continuing activities that began 112 years ago. The Bank's predecessor, the Anglo Palestine Company, was established in London in 1902 by Otsar Hityashvuth HaYehudim Jewish Colonial Trust Limited, the predecessor of Otsar Hityashvuth HaYehudim B.M.[1]

The Bank is defined as a banking corporation under the Banking (Licensing) Law, 1981, and holds a banking license under that law. As a "bank" and a "banking corporation" the Bank's activities are governed and delineated by a system of laws, orders and regulations, including, *inter alia*, the Banking Ordinance, the Bank of Israel Law, the Banking (Licensing) Law and the Banking (Service to Customer) Law, as well as by directives, rules, instructions and position papers of the Supervisor of Banks.

The Leumi Group is involved in a variety of banking, financial and non-banking activities, in Israel and overseas. The Group's activities are carried out through the Bank and subsidiaries and companies included on equity basis, through 274 branches located throughout Israel, and through 52 branches, agencies and representative offices in 15 countries throughout the world.

The Group's policy, in Israel and overseas, is to provide its customers with comprehensive banking and financial solutions and a high level of professional service, to enable them to make use of varied distribution channels and to offer them a wide variety of products, adapted to their needs.

As a leading banking group, aiming to achieve high levels of long-term profitability, Leumi constantly scrutinizes trends and changes in the business environment in which it operates and formulates strategies to deal with these changes.

To implement its strategy, the Bank is organized into five lines of business, concentrating on different market segments, with each business line specializing in providing banking and financial services to a particular customer segment:

Corporate banking concentrates on servicing major and international companies; commercial banking concentrates on servicing middle market companies; international and private banking is aimed at high net worth customers requiring highly sophisticated investment solutions; retail banking concentrates on providing banking services mainly to households and small businesses; and capital markets and financial management coordinates the activities of all the dealing rooms and the *nostro* under one roof, with a view to improving and expanding the range of services to customers who are active in the capital and financial markets, including institutional customers.

---

[1] Otsar Hityashvuth HaYehudim B.M. was the controlling shareholder of the Bank until the equalization of voting rights in the Bank in 1991. In 1993, most of the shares of the Bank passed to the ownership of the State, under the Bank Shares Arrangement Law (Temporary Provision), 1993. On 3 September 2007, the company ceased to be an interested party in the Bank.

Some of the financial services are provided by means of subsidiary companies that operate in various fields, such as: credit cards, retail and underwriting.

Furthermore, the Group invests in non-banking corporations operating in the various fields inside and outside Israel. The management of the non-banking investment portfolio is conducted through the subsidiary, Leumi Partners Ltd.

The Leumi Group operates in a competitive market in all its operating segments. The main competitors are currently other Israeli banks, although, in certain segments, there are additional competitors whose numbers are constantly growing, such as overseas banks and non-bank competitors, for example, insurance companies and other institutional entities.

In 2013, the fear of the repercussions of a crisis including the write-off of countries' debts in Europe receded, alongside a continuation of the economic stabilization of the economy of the United States. Nevertheless, GDP growth rates continue to be low in the developed countries and growth in developing countries has also been low compared to previous years. The Israeli economy grew in real terms by some 3.3%, including the effect of gas discoveries, compared to 3.4% in 2012. For further details, see the Economic Review below.

Total assets under management of the Group (both balance sheet and off-balance sheet*) amounted to NIS 1,086 billion as at 31 December 2013, as compared with NIS 989 billion at the end of 2012, an increase of some 9.8%, resulting primarily from an increase in the scope of activity and an increase in market values.

* Total assets, as well as customers' securities, the value of securities in custody of mutual funds, provident funds and supplementary training funds for which operational, management, custodial and pension counseling services are provided.

Below are principal data:

	As at 31 December				
	2013	2012	2011	2010	2009
Balance sheet data (NIS millions):					
Total assets (total balance sheet)	**374,360**	376,160	365,854	328,322	321,910
Credit to the public, net	**240,874**	241,264	241,320	223,981	204,669
Securities	**63,735**	56,408	47,936	55,791	57,505
Cash and deposits in banks	**44,351**	54,621	53,044	30,052	42,933
Investment in companies included on equity basis	**1,689**	2,129	2,270	1,924	2,178
Deposits of the public	**286,003**	289,538	279,404	249,584	250,418
Debentures, notes, and subordinated notes	**25,441**	27,525	29,999	26,939	25,261
Equity attributable to shareholders of the banking corporation	**26,425**	24,921	23,374	23,293	21,532

Below are principal data for the years ended 31 December:

	For the year ended 31 December				
	2013	2012	2011	2010	2009
Income, expenses and profit (in NIS millions):					
Net interest income	**7,357**	7,408	7,107	6,972	6,511
Expenses in respect of credit losses	**268**	1,236	734	584	1,521
Total non-interest income	**5,517**	4,774	4,175	4,767	5,107
Of which: commissions	**4,188**	4,199	4,116	4,129	3,890
Total operating and other expenses	**8,933**	9,100	8,341	7,961	6,781
Of which: salary expenses	**5,174**	5,290	5,061	4,686	3,896
Profit before taxes	**3,673**	1,846	2,207	3,194	3,316
Provision for taxes	**1,391**	811	418	1,241	1,272
Net profit attributable to shareholders of the banking corporation	**1,947**	931	1,891	2,334	2,089
Net profit per share attributable to shareholders of the banking corporation (in NIS)	**1.32**	0.63	1.28	1.58	1.42
Total profit for the period attributable to shareholders of the banking corporation	**1,458**	1,588	1,659	*	*

* Data of the total profit for the period attributable to shareholders of the banking corporation were presented from 2011.

Below are principal financial ratios (in %):

	As at 31 December				
	2013	2012	2011	2010	2009
Credit to the public, net, to total balance sheet	**64.3**	64.1	66.0	68.2	63.6
Securities to total balance sheet	**17.0**	15.0	13.1	17.0	17.9
Deposits of the public to total balance sheet	**76.4**	77.0	76.4	76.0	77.8
Deposits of the public to credit to the public, net	**118.7**	120.0	115.8	111.4	122.4
Total equity to risk assets (a)	**14.82**	14.87	14.34	14.96	13.90
Tier I capital to risk assets	**9.43**	8.55	8.07	8.43	8.20
Equity (excluding non-controlling interests) to balance sheet	**7.1**	6.6	6.4	7.1	6.7
Net profit to average equity (excluding non-controlling interests)	**7.6**	3.8	8.3	10.3	10.8
Rate of provision for tax on the profit before taxes	**37.9**	43.9	18.9	38.9	38.4
Expenses in respect of credit losses to credit to the public, net	**0.11**	0.51	0.30	0.26	0.74
Of which: expenses in respect of collective allowance to credit to the public, net	**0.11**	0.13	0.15	0.02	0.03
Expenses in respect of credit losses to total risk of credit to the public	**0.07**	0.34	0.20	0.17	0.48
Interest income, net to total balance sheet	**1.97**	1.97	1.94	2.12	2.02
Total income to total assets (b)	**3.44**	3.24	3.08	3.58	3.61
Total income to total assets managed by the Group (b) (c)	**1.19**	1.23	1.26	1.32	1.49
Total operating and other expenses to total assets	**2.39**	2.42	2.28	2.42	2.11
Total operating and other expenses to total assets managed by the Group (c)	**0.82**	0.92	0.93	0.90	0.87
Net profit to total average assets (c) (d)	**0.57**	0.26	0.56	0.73	0.58
Interest margin (e)	**2.08**	2.08	2.12	2.58	2.08
Operating and other expenses (without early retirement) to total income (b)	**68.8**	72.0	73.9	67.82	58.37
Non-interest income to operating and other expenses (without early retirement)	**62.3**	54.39	50.05	59.88	75.31
Non-interest income to total income (b)	**42.9**	39.19	37.01	40.61	43.96

(a) Capital – with the addition of noncontrolling interests, net of investments in the capital of companies included on equity basis and sundry adjustments.
(b) Total income – net interest income and noninterest income.
(c) Including off balance sheet activity.
(d) Average assets are total income-producing and other balance sheet assets.
(e) Data for 2009-2010 have been calculated according to the old format. The interest gap excludes the effect of derivatives and includes exchange rate differences.

Net profit attributable to the shareholders of the banking corporation (hereinafter: the net profit) amounted to NIS 1,947 million in 2013 compared to NIS 931 million in 2012, a fall of 109.1%.

The increase in net profit is mainly explained by an increase in noninterest income amounting to NIS 743 million, a reduction in respect of credit loss expenses amounting to NIS 968 million and a decrease in operating and other expenses amounting to NIS 167 million. On the other hand, an increase in net interest income amounting to NIS 51 million, an increase in the provision for tax amounting to NIS 580 million and a fall in the Bank's share in the profits of companies included on equity basis after the effect of tax amounting to NIS 226 million partially offset the abovementioned effects.

The profit in the fourth quarter of 2013 amounted to NIS 348 million, compared to a loss of NIS 259 million in the corresponding period last year.

The increase in net profit in the fourth quarter of 2013 is mainly explained by a decrease in expenses in respect of credit losses amounting to NIS 231 million, a fall in operating and other expenses amounting to NIS 357 million, mainly as a result of expenses that were and are likely to be in connection with the U.S. customers which were recorded last year and from a decrease in the Bank's share in the losses of companies included on equity basis after the effect of tax amounting to NIS 34 million.

Net profit per share attributable to the shareholders of the banking corporation was NIS 1.32 in 2013, compared with NIS 0.63 in 2012, and NIS 0.24 in the fourth quarter of the year, compared with a loss per share of NIS 0.18 in the corresponding period last year.

Return on capital in 2013 was 7.6% compared with 3.8% in 2012. The return on capital in the fourth quarter of 2013 was 5.4% compared with a loss on capital of 4.0% in the fourth quarter of 2012.

Total profit after the effect of tax (in addition to the net profit including also adjustments in respect of the presentation of available-for-sale securities at fair value and adjustments from the translation of financial statements) in 2013 amounted to NIS 1,458 million, compared to NIS 1,588 million in the corresponding period last year. In the fourth quarter of 2013, the total profit amounted to NIS 326 million, compared with an overall loss of NIS 89 million in the corresponding period last year.

The following table presents the contribution of the profit centers in the Group to the net profit attributable to the shareholders of the banking corporation:

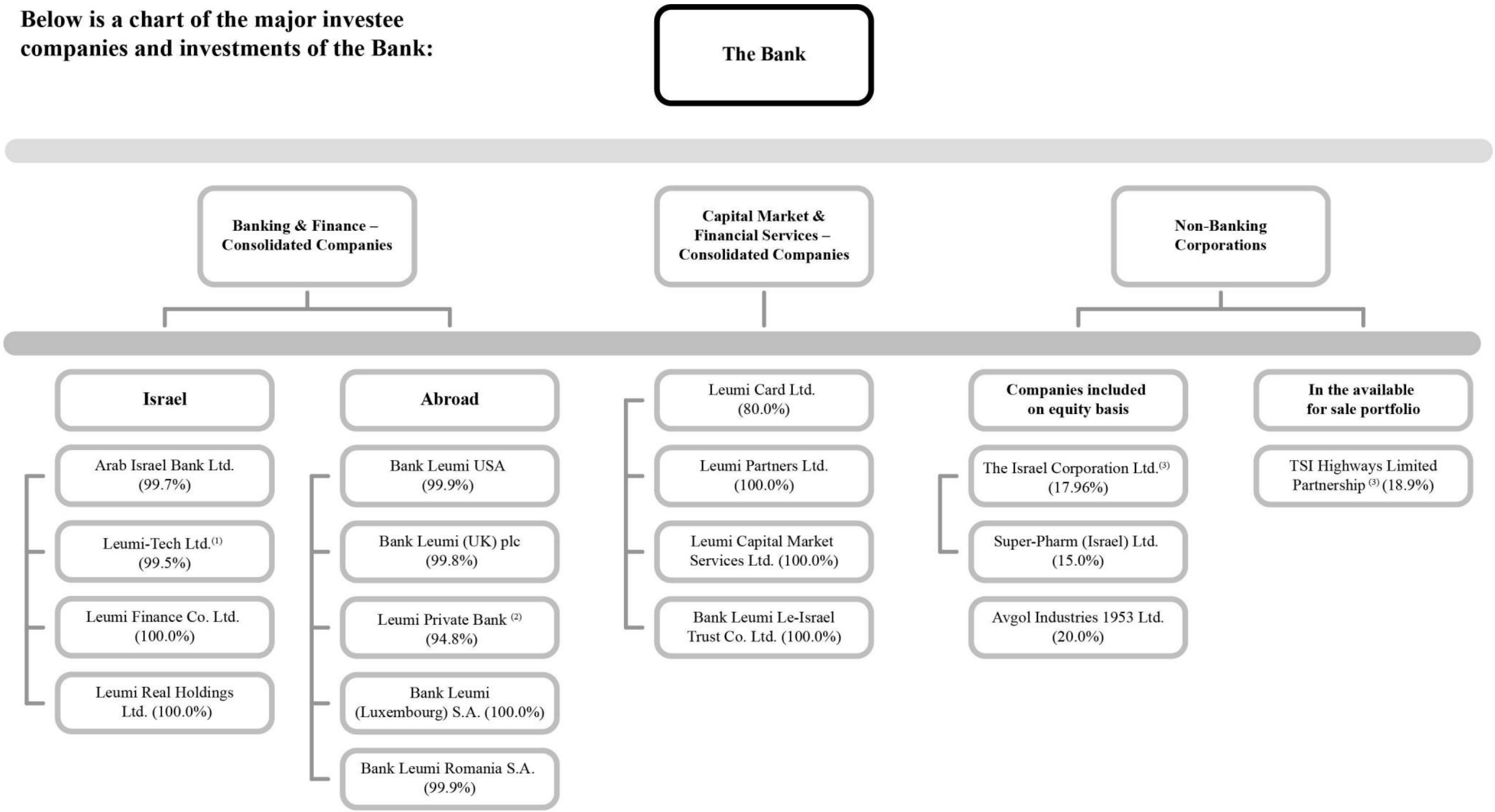
	2013		2012	
	Total investment	Contribution to net profit	Total investment	Contribution to net profit
	NIS billions	NIS millions	NIS billions	NIS millions
The Bank (1)	**15.2**	**1,775**	13.5	330
Subsidiary companies in Israel (2) (3)	**5.3**	**556**	4.8	562
Overseas subsidiary companies	**4.6**	**(52)**	4.9	143
Companies included on equity basis	**1.3**	**(332)**	1.8	(104)
Total	**26.4**	**1,947**	25.0	931

(1) Total investment includes the activity of Leumi Mortgage Bank which merged with Leumi on 31 December 2012.

(2) The contribution to net profit for 2013 includes the profits of Leumi Mortgage Bank which merged with Leumi on 31 December 2012. The profits of Leumi Mortgage Bank in 2012 amounted to NIS 303 million and were included within profits of subsidiaries in Israel.

(3) Includes the profit and/or loss of companies included on equity basis of Leumi Partners Ltd.

Below is a chart of the major investee companies and investments of the Bank:



(1) Formerly Leumi Leasing & Investments Ltd.
(2) 98.6% in voting rights.
(3) 18.13% in voting rights.

Basel II General (Table 1 – Basel II)

a. Bank Leumi Le-Israel Ltd. ("Leumi") whose office is situated in Tel Aviv, Israel, is the parent company of the Leumi Group.

b. The table on the previous page presents a chart indicating the structure of the Group and its principal investee companies.

For further details in respect thereof, see the chapter below, "Description of the Group's Business according to Segment and Area of Operations" and Note 6 to the financial statements.

The consolidation of the consolidated companies and the recording of the equity value of the companies included on equity basis are in accordance with generally accepted accounting principles and in accordance with the regulations of the Bank of Israel. However, in calculating the regulatory capital, goodwill, intangible assets and investments in unconsolidated banking and financial subsidiaries (some NIS 377 million) are deducted from the accounting capital.

c. The main regulatory limits on the transfer of liquid funds between Group companies in Israel and abroad are:

1. The Bank of Israel does not limit the placement of deposits by the Bank in Group companies in Israel and abroad. However, it has placed restrictions on capital investments by the Bank in companies in Israel and abroad. Every material investment requires the prior approval of the Bank of Israel.
2. Directives of authorities in the United States restrict local banks in the extent of their exposure of any kind *vis-à-vis* related companies. The maximum rate of exposure to a related company is 10% of the Bank's capital in the United States, and *vis-à-vis* the group of which the Bank is a member in the United States, the maximum rate is 20% of its capital.
3. Directives of the authorities in the United Kingdom restrict local banks in the amount of exposures of any type *vis-à-vis* related companies. The maximum rate of exposure towards the Group (except for Leumi and the subsidiary in Jersey) is 25% of the Bank's capital in the UK. The maximum rate of exposure towards Leumi and Bank Leumi (Jersey) is 100% of the Bank's capital in the UK.
4. Directives of the authorities in Switzerland require the bank in Switzerland to deduct deposits in the group from the capital by amounts exceeding 25% of the Bank's capital in Switzerland.

Merger between the Bank and Leumi Mortgage Bank Ltd. ("Leumi Mortgage Bank")

On 9 September 2012, the Board of Directors of the Bank approved the merger of Leumi Mortgage Bank with the Bank. On 10 September 2012, the Board of Directors of Leumi Mortgage Bank approved the implementation of the said merger. The merger took place on 31 December 2012 ("the Merger Date"). See Immediate Reports dated 10 September 2012 (ref. no. 2012-01-234537 and 2012-01-234585).

According to the merger agreement, Leumi Mortgage Bank, which was a wholly owned and controlled subsidiary of the Bank, merged with the Bank.

The merger which was executed is a statutory merger, whereby Leumi Mortgage transferred its assets and liabilities to the Bank, and Leumi Mortgage was dissolved without liquidation, pursuant to the provisions of Chapter 1 of the Eighth Part of the Companies Law, 1999, and subject to the provisions of Chapter 2, Part E2 of the Income Tax Ordinance, such that on completion of the merger, Leumi Mortgage ceased to exist.

With effect from 15 January 2013, the banking license of Leumi Mortgage Bank was canceled.

Aims of the merger:

The merger serves both a business and an economic purpose, viz., to enable the Leumi Group to increase the level of group synergy between retail and mortgage operations. The purpose of the move is to allow the Bank to provide retail customers with a value proposition appropriate to all of their needs, *inter alia*, in view of the improvement in the level of the product offered to customers, with an emphasis on providing a variety of services to the customer, while reducing Group expenses and utilizing the sales floor more effectively.

Business Strategy

Leumi's Vision

During 2013, the Board of Directors and management of Leumi led a comprehensive and intensive process to refresh the Bank's vision and core values. The goal of refreshing the vision grew from the desire to define a vision that would match the spirit of the period which the Bank's employees could harness.

The process that took place in refreshing the vision included examining trends that influence Leumi's activity, analyzing the way in which leading banks and organizations around the world define their vision and holding internal workshops in senior forums, in the Bank management and the Board of Directors.

Leumi's vision, as defined in 2013, is as follows:

"To lead proactive and innovative banking on behalf of the customer"

At the basis of the vision is the aspiration to devise a dynamic system, which combines the Bank's values with product and technological innovation – a system which will be, for the Bank's customers, a place in which they can find the best and most suitable solution for their financial requirements, and, in so doing, derive a fair profit, maintain the Bank's stability and create a balance between the needs of the employees and the expectations of the shareholders. As a financial group, with major influence over the business and public culture in Israel, Leumi considers its commitment to the community to be a social and ethical anchor, which it will continue to nurture.

Background Conditions

The competitive and business environment in which the Bank operates is complex and is influenced by several exogenic factors. The financial markets around the world and in Israel, regulation in Israel and abroad, and changes and trends in areas such as technology and the customers' preferences affect Group activity and the strategy derived as a result thereof.

For information on the macro-economic environment in Israel and around the world, see the chapter, "Principal Developments in the Economy in the Report of the Board of Directors", below.

Increased regulation

The impact of regulation on the banking sector continues to expand in Israel and throughout the world. The financial crisis has further increased the power of the regulator and all the various aspects of supervision and has become a key element in the stabilization of the financial system.

Besides the local regulatory activities, the banks are also affected by global regulation. In 2011 the provisions of Basel III were published, further toughening the capital adequacy requirements and adding more requirements for maintenance of liquidity. Additional laws have been published affecting the international banking model. An example is the Foreign Account Tax Compliance Act (FATCA), which was enacted in the United States and requires banks around the world, including those in Israel, to report on the accounts and assets of American customers. Furthermore, regulation in activity in derivatives in the United States (Dodd-Frank) and in Europe (EMIR) is liable to impact the Bank indirectly through the counterparties to derivative transactions. In addition, the enforcement of legislation of various countries on cross-border activity and activity *vis-à-vis* foreign residents continues to be increased.

Public pressure and the characteristics of a macro-economic environment also give entrepreneurs unprecedented scope on the part of the regulators in Israel. Major local initiatives include the Zaken Committee for the Encouragement of Competition, which led to decisions whose implementation is of great significance to the banks' activity, the Concentration Law, which was enacted and is expected to lead to changes in ownership and control of financial and non-bank entities and in the banks' ability to invest in non-banks entities, and the reform to reduce and restrict distribution fees, which has been approved by the Finance Committee.

In addition to the restrictions regarding income, increased regulation creates material pressures for banks in terms of costs and inputs required for careful preparation and compliance with directives.

In addition, regulation has an impact on competition and growth of the banking system in Israel, as it restricts banks' ability to expand activity through acquisitions and mergers or to enter into new areas of operation.

The consumer environment

In the summer of 2011, a social protest erupted in Israel, for the first time, led mainly by the Israeli middle class. This transformed public discourse within Israel and put the socioeconomic issue on the public agenda.

The protest expressed the "spirit of the times" and broke out at the same time as similar protests throughout the world, against the backdrop of the aspiration to narrow societal gaps, reduce the cost of living and provide better opportunities for the whole population to develop, both economically and socially.

In its early stages, the social protest was not directed against the banks. However, as large corporations are involved in almost everything that happens in the Israeli economy, the banks, among them, Leumi, were continually a part of this discourse.

When the "tent protest" finished in September 2011, the protest gradually began to change its approach, moving increasingly from the street to the political arena and to the media. As a rule, the social media, which was the fuel for the protest, led to the phenomenon called "the availability of influence", so that to distinguish it from previous periods, everyone in the public now had a tool with which he could influence the course of events.

More so than in the past, the customer today expects banking that he considers fair and more available and accessible, simpler and more transparent. As mentioned above, the customer has high consumer awareness and is linked to other consumers, particularly through social networks. He is also aware of his purchasing experience, a fact which gives him know-how and a large amount of bargaining power. The customer consumes information and services through a wide array of digital and physical channels and expects a consistent service experience using the various interfaces with the Bank.

The strengthening of the impact of technological innovation may be seen in consumer trends, foremost of which is the Smartphone revolution (smart cellular phones). The ever-increasing use of Smartphones around the world, and in Israel, in particular, alters consumer habits, the mode of payment, the purchasing experience, the purchasing location, etc. The consumer is continually connected and expects to receive services and information in every place and at any time of day, in line with his choice and preferences.

Competitive environment

Domestic banks

In 2013, the trend of increase in the level of competition in all of the banking sectors of activity continued. The domestic banks continue to focus on households (*inter alia*, through mortgages) and in the small and medium business segments. They are taking steps to enroll new customers and increase the scope of activity, and focus efforts on developing value proposals based on customer clubs, improving technological tools for reinforcing the customer experience in establishing new multi-channel service models and improving their operating efficiency.

Competing non-banks

Loans by institutional entities – In recent years, there has been a clear trend of increasing loans of institutional entities to the business sector. These loans are characterized by large amounts, and are therefore, in most cases, designated for large corporations. In addition, as a part of the trend of institutional entities to grant direct loans, there has been a trend of granting finance to projects of rental properties, and residential properties with support (together with the commercial banks). Against the backdrop of the increase in the volume of activity, the Goldschmidt Committee was set up, and in the past year, it published interim recommendations for regulating the activity of the institutional entities in the field, taking into account the mechanisms of control, risk management, duty of reporting and disclosure, etc.

Activity in the capital market and in brokerage – Traditionally, most of the competition in these areas of activity is by investment houses and other managing entities (provident funds, training funds, insurance, etc.). The competition is focused on institutional customers, companies and business customers and private banking/affluent customers. In recent years, the banks have begun to re-establish their status in the area, particularly with institutional and business customers, in light of their ability to offer customers an overall value proposal. Among the investment houses, there was a marked trend of consolidation, with investment houses merging, and their number in the market declining. It is estimated that in view of the erosion in the rate of profitability of the investment houses from their traditional activity, they are likely to look for new channels of activity, and even compete directly and more significantly in areas that have traditionally been controlled by the banks.

Technology-based players – In recent years, with the expansion in consumers' use of advanced technology (particularly smart mobile phones), the supply and quality of ventures/developments offering high-tech based financial services are becoming greater and greater (Fintech). These ventures do not represent overall competition to the traditional banks, but certainly they gnaw away at the banks' share in certain areas of activity – payments, money transfers, financial investments and securities trading, loans, savings and financial management services.

Internet and social bank models – In recent years, the trend of setting up Internet banks, a large proportion of which are being established by the traditional banks themselves, has become widespread, These banks offer a basket of services in direct channels (with restricted access or no access at all to the branch) and are focused on retail customers who are interested in an advanced digital service experience, together with attractive price offers. In addition, various enterprises have recently been promoted in Israel to set up a bank with "social" features. The most advanced initiative in this area has been "Ofek – Capital Cooperative Association", which is expected to operate as a cooperative bank.

Leumi's strategy

In order to realize Leumi's vision, and in accordance with the changes in the business environment, the Leumi Group has managed a comprehensive process for focusing and refreshing the Group's strategic goals.

Although Leumi strives to adapt its activities to its strategy, and to achieve excellence in all of the areas in which it operates, strategic planning, by its nature, involves a fair amount of uncertainty. The achievement of the strategic plan depends on many variables, including: the state of the markets in Israel and abroad, the security situation and the ongoing effects of regulatory changes, the extent of whose effects in the long term cannot yet be defined with certainty.

In order to ensure continued growth and profitability in the long-term, Leumi is focusing its strategic efforts and its resources - capital, human and managerial - on business areas that generate the highest yields and profitability, while taking steps to improve profitability in areas where the level is lower. Additionally, Leumi is investing in building up its abilities in order to ensure good results in the long-term.

Leumi Group has defined five strategic goals, which express the aspirations and administrative focus in Leumi for the medium to long term. The five strategic goals may be divided into two main groups – two goals relating directly to the business lines (numbered 1A and 1B) and three goals dealing with the principal levers whose attainment of a strategic focus is crucial (numbered 2, 3 and 4 – with no importance given to their order of presentation).

The principal strategic goals of Leumi are:

1A. Upgrading the service model and value proposals – focusing on retail, in small and medium businesses and on high-tech.

1B. Adaptation of the model of activity of the Corporate Department and the Real Estate Department – focusing on exploiting Leumi's competitive advantages under changing conditions (non-banking and banking)**.**

2. Assimilation of an organizational customer-centered culture – focusing on training and motivating employees of the organization in line with the Group's core values and vision.

3. Improving efficiency and flexibility – focusing on the human resource, information technology and procurement.

4. Creation of a qualitative and innovative technological environment – focusing on strengthening business performance and the Bank's ability to respond rapidly to constant changes in the activity environment.

Group strategy is implemented in accordance with the risk appetite approved by the Board of Directors, alongside the use of advanced procedures and tools for managing the different types of risk, and the completion of preparations for regulatory requirements, including those of Basel III.

The Group's targets have been adapted to the lines of business in which Leumi operates, which are outlined below. Each business line is specialized in a defined section of the market and its purpose is to create a relative advantage among its target population.

Savings and efficiency

With effect from 2012, a streamlining program represents a central pillar in Leumi Group's work plan. The aim of the program is to lead to material savings in the Group's operating expenses and an improvement in its efficiency ratio on a continuing and long-term basis. The program includes steps in the area of human resources and in other material expenditure areas including:

- A reduction in the workforce based on natural retirement and a reduction in the intake of employees, which is a consequence of streamlining measures and structural measures, such as the "Advancing Together" project, in which back-office activities have been transferred from the branches to the centers of expertise and efficiency in the Bank's offices. The streamlining measures and the reduction in the workforce also made possible a corresponding reduction in the amount of space the Bank uses and in the related expense through the sale of assets that became redundant and the vacating of rented premises.

- In addition to a reduction in the area used by the Bank, steps are being taken to utilize areas effectively, including examining the location of the Bank's sites for optimizing rents for business activity and municipal rates.

Some of the information in this chapter is "forward looking information". For the meaning of this term, see the section, "Description of the Banking Corporation's Business and Forward-Looking Information", below.

Control of the Bank

With effect from 24 March 2012, the Bank is defined, according to the provisions of the law, as a banking corporation without core control and there is no shareholder who is defined as a controlling shareholder in the Bank.

For updated information regarding the holdings of interested parties in the Bank, see Immediate Report on the Holdings Position of Interested Parties and Senior Officeholders, dated 6 March 2014 (ref no. 2014-01-007785).

Description of Operating Segments

The Bank in Israel is organized into five lines of business. Each business line specializes in the provision of service to segments of customers with similar characteristics and needs. This specialization allows for the provision of a high level of professional service. In addition, there are a number of management units that provide various services to the business divisions.

The subsidiary companies in Israel and abroad have been assigned to the relevant business line within the Group according to the nature of their activities and the characteristics of their customers.

The following are details of the Bank’s five major lines of business:

Retail banking deals with private and small business customers. The aim of retail banking is to provide a multi-channel, integrative customer experience in the branch channel and in the direct channels (Leumi CALL, the Internet, cellular, electronic terminals, information booths and ATM's), supported on a modern, operational service model, adapted to customer requirements. The main strategic goals of retail banking are to expand the customer base in operating segments which have potential, and increase activity levels with customers by continually improving the level of service and adapting value proposals to the needs of the customer in accordance with his way of life.

Commercial banking deals with middle-market business customers and their interested parties. The strategic goal of commercial banking is to continue to strengthen its leading position by expanding the volume and range of activities with existing customers and by recruiting new customers, whilst providing a range of financial services required for its customers operating in Israel and abroad.

Corporate banking deals with the project support and financing of the segment of large business customers and multi-national corporations, including entrepreneurial and contract companies involved in large projects in the area of real estate and infrastructure. Among those managed in the Corporate Department and Real Estate Department are customers whose business activity is complex, whose business is international and/or whose activity is managed in several of the Bank's overseas subsidiaries. The objectives of corporate banking are to provide the entire spectrum of customers with all necessary financial services, while involving the various units in the Leumi Group, in Israel and abroad, as necessary, so as to increase the variety of products and services offered to customers.

Private banking deals with wealthy private customers in the Group, both in Israel and abroad. Activities are carried out through specialist centers in Israel that are designated for foreign and Israeli residents and also through the Bank's subsidiaries in the USA, the UK, Switzerland and Luxembourg.

Capital markets banking and financial management deals with the management of the Bank’s *nostro* and the operation of all the Bank’s dealing rooms for the purpose of securities trading and brokerage activities in currencies, interest rates, derivatives and securities. Financial management includes the development of financial and investment products, management of the Bank's assets and liabilities (ALM) and in the management of investments in financial assets. The division also manages the relationship with overseas financial institutions and is responsible for providing services to customers in Israel active in the capital and money markets, including institutional customers.

Principal Operating Segments

Pursuant to Bank of Israel directives, an operational segment is a component which has three characteristics:

1. It engages in business activities from which it is likely to produce income and bear expenses (including income and expenses from transactions with other segments at the Bank);

2. Its operating results are regularly examined by the Management and the Board of Directors in order to make decisions relating to the allocation of resources to the segment and the appraisal of its performance;

3. There is separate financial information with regard to the segment.

The principal operating segments that have been determined under the directives of the Bank of Israel in accordance with the said characteristics are as follows:

1. Households - providing comprehensive banking services to households and private customers, at every stage of life.

2. Small Businesses - providing banking services to small businesses and local authorities.

3. Corporate Banking - providing banking and financial services to the major and international companies for their operations in Israel and abroad.

4. Commercial Banking - providing banking and financial services to the middle market companies and their interested parties.

5. Private Banking - providing local and global financial services and solutions to private customers resident in Israel and abroad with large financial asset portfolios.

6. Financial Management and Capital Markets - the *nostro* activities and dealing rooms and the provision of services to institutional customers and foreign financial institutions, including the operating results of investments in (non-banking) companies included on equity basis and investment in shares in the available-for-sale portfolio.

7. Others - activities not assigned to other segments. This includes other activities of the Group, none of which constitutes a profit segment according to the directives of the Supervisor of Banks.

Segmented operations also include inter-segment activity, such as services that are provided to customers of another segment as well as activities (derived from products) such as mortgages, credit cards, capital market and real estate.

For further details, see below the chapter, "Operating segments in the Group" and note 27 to the financial statements.

a. The criteria for the attribution of customers according to the operating segments at the Bank in Israel are generally as follows:

Business Customers:

Segment	Scope of obligo	Business turnover of borrower
Corporate Banking	above NIS 120 million*	above NIS 400 million
Commercial Banking	above NIS 10 million and up to NIS 120 million (inclusive)*	above NIS 20 million and up to NIS 400 million
Small Businesses	up to NIS 10 million (inclusive)	up to NIS 20 million

* The corporate banking segment will also handle customers with a facility of more than NIS 80 million, where they have an overall obligo in the banking system exceeding NIS 250 million.

Private Customers:

Segment	Israeli residents	Overseas residents
	Financial wealth	
Private Banking	above NIS 6 million	above US$ 0.5 million
Households	up to NIS 6 million	up to US$ 0.5 million
Commercial Banking	up to NIS 6 million	up to US$ 0.5 million

It should be noted that attribution to a specific operational segment is sometimes carried out in accordance with additional criteria to those indicated above – e.g. the size of the obligo with regard to corporate customers, and financial wealth, with regard to private customers. Criteria such as the nature of a corporation's business operations and the scope of its business, such as international trade volumes, complex and special transactions, complex projects and construction financing, can change the segmental attribution of a certain customer.

As stated above, the Bank is organized according to lines of business, and its policy is to attribute customers – as far as possible – to the appropriate business line/operational segment, according to the customers' characteristics and activities. Nevertheless, it should be noted that segmental attribution is determined according to the sector in which a customer's account is actually operated. As long as segmentation has not been carried out among the segments, the segmental classification does not change, and the financial results in respect of the customer are recorded in the segment in which the customer's account actually operates.

b. The banking subsidiaries have been attributed to the operating segments as follows:

- The Arab Israel Bank Ltd. – to households, small businesses, commercial banking and financial management.
- Leumi USA – to commercial banking, private banking and financial management.
- Leumi Private Bank (Switzerland) and Luxembourg – to private banking.
- Leumi UK – to households, commercial banking, corporate banking and private banking.
- Leumi Romania – to households, small businesses, commercial banking and private banking.

The segment data provided here, on a consolidated basis, is the result of a summarization of the segments based on the segment definitions within each of the Group's organizations, which are not identical in terms of size. In terms of materiality, the Bank generally constitutes some 80% of each segment.

Financial Measurement System

Objectives of the system:

- Measuring the profitability of the various profit centers;
- Measuring the business activity volume of the various profit centers according to various classifications;
- Measuring performance against the goals in the work plan;
- Uniformity in analyzing the business activity;
- Overall control of the business activity and the profitability from such activity;
- Directing the business units and branches to achieve the Bank's targets, including profitability targets;

- To provide a tool for allocating the Bank’s resources in a rational manner, on the basis of cost-benefit analysis;

- To provide a basis for appraisal and remuneration.

The way in which income and expenses are attributed by operating segment in the Bank is obtained as follows:

The basis of the Bank’s existing system ("the Bahan system") is the "data warehouse" that centralizes all the Bank’s transactions and, with the assistance of an appropriate index, enables transactions to be sorted and classified between the various profit centers.

The data presented below regarding operating segments includes the Bank's data according to the principles of the "Bahan" system as explained below, while the segmented data of the subsidiaries in Israel and abroad has been taken from their financial statements, and as defined by them.

In measuring the profitability of overseas subsidiaries, the exchange rate differentials after the effect of taxes arising from financing the investment in overseas subsidiaries are allocated to the net interest income of the overseas subsidiaries, whose functional currency, for the purposes of the consolidated statements, is identical to the functional currency of the Bank.

Net interest income **-** The profit center is credited with the interest received from the loans that it extended, or is debited with the interest that is paid on deposits it raised.

At the same time, the profit center granting the loan is debited, and the profit center receiving the deposit is credited with transfer prices. The transfer prices are usually determined according to market prices following certain adjustments and generally reflect risk-free returns or the marginal costs of raising funds with the same linkage sector and currency and for a similar term. The effects arising from exchange rate differentials between the shekel/foreign currencies, and also changes in the CPI on surplus uses and/or sources are attributed in the Group to the financial management segment. Using the method described above, the profit centers bear credit risks but do not bear market risks.

The profit and loss statements of each of the segments also take into account the capital allocated to the segment. Every profit center is credited in respect of the Tier 1 capital that was allocated to it in respect of the risk assets in accordance with risk-free yield and is charged in respect of the additional cost of the Tier 2 capital. In this way, the available capital attributed to the segment is credited with interest equal to the marginal cost of raising funds in accordance with the segment that it is financing, or invested in the capital market.

The interest income from the management of the *nostro* is reflected in the financial management and capital markets segment.

Expenses in respect of credit losses are charged to the profit center in which the customer’s account is managed. The same applies to the collective allowance required pursuant to the directives of the Bank of Israel.

Noninterest income

All of the noninterest income (noninterest financing income, commissions and other income), which the Bank charges its customers and/or subsidiaries in respect of various services, is credited to the profit center in which the customer’s account is managed. Income from *nostro* securities, profits of the severance reserve and dividends that the Bank receives are credited to the financial management and capital market profit center.

Expenses

Expenses are attributed to the lines of business (divisions and departments in the Bank) according to the segmental association of the customers dealt with in those lines of business.

In a minority of cases in which a line of business operates in several operational segments, expenses of lines of business are attributed to relevant segments and products on the basis of the multi-dimensional pricing of transactions. Pricing is a system in which the cost of the transaction is calculated taking into account the type of transaction, the type of customer making it and the channel in which the transaction is executed.

Expenses not connected with the direct activities of the profit center (operational segment), such as expenses in connection with the actuarial pension liability, are not charged to the profit centers, but are reflected in the Financial management and Others segment.

For further details regarding operating segments, see the chapter, "Operating segments in the Group" and note 27 to the financial statements.

Measuring the return on capital

In intensifying the measurement of the units' performance and adapting it for the unique characteristics of risk for each unit, the rate of return on risk-adjusted capital (RORAC) of operational segments and their contribution to the Group's profit (economic value added - EVA) is measured, taking into account the cost of capital according to the multi-year return approved by the Board of Directors. The allocation of capital to risk components among the segments is carried out in accordance with the various risk characteristics inherent in each segment, in accordance with Basel II.

The allocation of First Pillar capital (in respect of credit, market and operational risks) is according to Basel II approach. Credit risks on the basis of weighted risk assets in the units, market risks and operating risks are calculated according to the standardized measurement method. Second Pillar Capital is allocated to the units divided into its various components according to models designed by the Bank.

The profit of the operational segments is adjusted for the risk capital in each segment. The risk-adjusted return was calculated as a ratio of the adjusted profit to the average shareholders' equity allocated to the sector, which constitutes a part of the risk capital allocated (First Pillar capital, Second Pillar capital and the balance of the capital in respect of extreme scenarios and retained earnings).

For each segment, the profit is calculated, taking into account the cost of Tier 1 and Tier 2 risk capital allocated to each segment. At the Group level, the value added for the shares (EVA) is the net profit, calculated as aforesaid, less the cost of the shareholders' equity, according to the required long-term return over the shareholders' equity, as determined by the Board of Directors.

Evaluating the performance of the units

The BSC (Balanced Score Card) is a management tool for managing the performance of the Bank and its lines of business in a variety of quantitative and qualitative matters which Bank management determined to be matters under focus in the framework of Leumi's strategic program.

Among other things, the following are measured within the BSC framework: finance and risk management (targets such as return-adjusted return, savings and efficiency and capital management), customer satisfaction, processes, capabilities and infrastructure.

The list of targets measured in the BSC framework and the weighting of each target are updated annually in accordance with emphases determined by Bank management in the framework of discussions of the work plan. Targets for the lines of business of the Bank are derived from the targets of the business lines and the other divisions in the Bank.

In the context of the focus on the subject of savings and efficiency which was implemented in 2012-2013, the measurement of relevant targets, for this subject in the BSC, was enhanced.

This system of measurement is discussed every year by the Remuneration Committee and in the Board of Directors and receives its approval, as it is, *inter alia*, a basis for evaluation and remuneration.

Capital Resources and Capital Adequacy

Capital attributable to the Shareholders of the Banking Corporation as at 31 December 2013 amounted to NIS 26,465 million, compared with NIS 24,921 million at the end of 2012, an increase of 6.0%. The increase in shareholders' equity mainly derives from the profit for the year, which was offset by a decrease in adjustments of available-for-sale securities portfolio and translation adjustment fund (other comprehensive income)**.**

Structure of components of capital for purposes of calculating the capital ratio – (Table 2 Basel II):

	31 December 2013	31 December 2012
	NIS million	
Tier 1 capital:		
Share capital	**7,059**	7,059
Premium	**1,129**	1,129
Retained earnings	**18,278**	16,296
Other capital reserves	**50**	58
Adjustments from translation of financial statements of investee companies	**(242)**	(85)
Capital reserve in respect of share-based payments and loans to employees for the purchase of shares of the Bank	**(30)**	(31)
Non-controlling interests in capital	**340**	307
Amounts deducted from Tier 1, including goodwill, investments and other intangible assets	**(321)**	(421)
Total Tier 1 capital	**26,263**	24,312
Tier 2 capital:		
45% of the amount of net profits, before the effect of relevant tax in respect of adjustments to fair value of available-for-sale securities	**100**	333
General provision for doubtful debts	**428**	428
Innovative and non-innovative compound capital instruments	**6,149**	6,071
Subordinated notes	**8,395**	11,227
Amounts deducted from Tier 2 capital	**(65)**	(81)
Total Tier 2 capital	**15,007**	17,978
Total capital base for purposes of capital adequacy	**41,270**	42,290

For further details see Note 13D to the financial statements.

In accordance with Basel II directives, the components of capital in the Bank for the purposes of calculating capital adequacy are divided into two tiers, Tier 1 capital and Tier 2 capital. The total of these tiers is called "the capital base for purposes of calculating capital adequacy".

The main characteristics of Tier 1 capital are as follows:

Tier 1 capital includes share capital, accumulated reserves, premium, capital reserve in respect of share-based payment transactions and others, other funds in respect of companies included on equity basis, adjustments from translation of autonomous investee companies abroad, less loans to employees for the purchase of the shares of the Bank, with the addition of rights not conferring control of capital (minority interests) and less goodwill, intangible and other assets and unrealized net losses (after tax) in respect of adjustments to fair value of available-for-sale securities. Tier 1 capital can include compound capital instruments. There are no compound capital instruments in this Tier in the Leumi Group. Tier 1 capital without compound capital instruments is called "core capital".

The main characteristics of Tier 2 capital are as follows:

Tier 2 capital includes 45% of the amount of unrealized profits, net (after the effect of tax) in respect of adjustments to fair value of available-for sale securities, general provision for doubtful debts, compound capital instruments (Upper Tier 2 capital) and subordinated notes up to the level of 50% of total Tier 1 capital (Lower Tier 2 capital). Total Tier 2 capital (upper and lower) is limited to 100% of Tier 1 capital.

Capital instruments included in Upper Tier 2

- Non-innovative compound capital instruments: subordinated capital notes issued for a period of at least 49 years. The issuer (only) can make an early redemption after 5 years provided that it will be replaced by an instrument of the same or higher quality. The capital instruments will be issued by Leumi or by means of issues by Leumi Finance.

- Innovative compound capital instruments: capital notes which meet the definition of non-innovative compound capital instruments and in addition include a step-up mechanism, which represents a stimulus for early redemption. A step-up mechanism which determines the rate of increase of interest to investors will be used only once, after at least 10 years from the date of issue.

Capital instruments included in Lower Tier 2

- Subordinated notes which were issued for a term of at least 5 years. Leumi raised subordinated notes directly, or by means of issues by Leumi Finance. The rights of the subordinated notes are subordinated to other creditors except for holders of Upper Tier 2 and Tier 1 capital instruments. In addition, Lower Tier 2 also includes non-negotiable subordinated deposits.

As well as that stated above, investments in unconsolidated banking and financial subsidiaries are deducted from both capital tiers and also deductions connected with securitization exposures.

With effect from 1 January 2014, the provisions of Basel III (updating the provisions of Proper Conduct of Banking Business nos. 201-211) came into force, altering the structure of the capital and the characteristics of its components. For a summary of the changes and effects, see below the chapter "Exposures to Risk and Methods of Risk Management – Basel Directives and Preparations in Leumi".

Shareholders' equity relative to total assets at 31 December 2013 reached 7.1% in comparison with 6.6% at 31 December 2012.

Capital adequacy structure

Equity to risk components ratio on 31 December 2013 was as follows:

According to Basel II - Pillar 1, the ratio of total equity to risk assets is 14.82%, compared to 14.87% at the end of 2012. The ratio of core capital to risk assets is 9.43%, compared to 8.55% at the end of 2012.

Capital adequacy - (Table 3 Basel II):

Risk assets and capital requirements in respect of credit risk deriving from exposures of:	**31 December 2013** Risk assets	Capital requirements (2)	31 December 2012 Risk assets	Capital requirements (2)
	NIS million		NIS million	
Sovereign debts	**788**	**71**	937	84
Debts of public sector entities	**2,242**	**202**	2,169	195
Debts of banking corporations	**4,372**	**393**	4,676	421
Debts of securities company	**35**	**3**	-	-
Debts of corporations	**128,756**	**11,588**	141,616	12,745
Debts collateralized by commercial real estate	**20,958**	**1,886**	23,260	2,093
Retail exposures to individuals	**26,639**	**2,398**	23,728	2,136
Loans to small business	**10,657**	**959**	9,611	865
Housing mortgages	**38,375**	**3,454**	33,474	3,013
Securitization	**831**	**75**	864	78
Other assets	**13,895**	**1,251**	13,560	1,220
Total in respect of credit risk (1)	**247,548**	**22,280**	253,895	22,850
Risk assets and capital requirements in respect of market risk (1)	**10,510**	**946**	9,710	874
Risk assets and capital requirements in respect of operational risk (1)	**20,426**	**1,838**	20,841	1,876
Total risk assets and capital requirements (3)	**278,484**	**25,064**	284,446	25,600
Total capital base for capital adequacy	**41,270**		42,290	
Total capital ratio	**14.82%**		14.87%	
Tier 1 capital ratio	**9.43%**		8.55%	

(1) Weighted risk assets according to the standardized approach in respect of the First Pillar only.
(2) Calculated according to the 9% minimum requirement.
(3) Additional capital buffers have been calculated in respect of the Second Pillar

Below is the capital adequacy ratio on a consolidated basis and for principal subsidiaries according to Basel II:

	31 December 2013	31 December 2012
Leumi – on consolidated basis	**14.82**	14.87
Leumi Mortgage Bank (1)	**-**	11.85
Arab Israel Bank	**12.50**	14.76
Leumi Card	**16.00**	16.00
Bank Leumi U.S.A. (2)	**14.54**	14.47
Bank Leumi UK	**16.39**	15.53
Leumi Private Bank	**44.91**	24.24

(1) The activity of the company was merged on 31 December 2012.
(2) The company is not required to be reported under Basel II principles, and the figures are according to United States regulations.

For further details in connection with the capital components, risk assets and the capital ratio of significant banking subsidiaries, see Note 13D to the financial statements.

Pursuant to a directive of the Supervisor of Banks, until the adoption of the Basel III directives, the overall capital ratio must not be lower than 8% in respect of Pillar 1 and 1% in respect of Pillar 2. Total minimum capital ratio is 9%.The capital adequacy ratios of Leumi for future years will be adapted to the long-term targets in accordance with Proper Conduct of Banking Business Regulation no. 201 regarding "Measurement and Capital Adequacy – Introduction, Incidence and Calculation of Requirements" which was published on 30 May 2013.

First Pillar – calculated at 8% of the total risk assets and includes credit risk, market risks and operating risks.

Second Pillar -"capital buffers" are calculated in respect of risks that are not included in the context of the First Pillar, such as: large borrower concentrations, group borrowers, sectoral concentrations, country risk, various market risks and capital buffers in respect of risks including in the First Pillar but in respect of which expansion is required.

Risk assets are calculated in the Leumi Group according to the standardized approach in the Basel II provisions.

Capital planning in the Leumi Group reflects a forward-looking view of risk appetite and the capital adequacy required as a consequence of this. Risk factors are further checked under strict assumptions of stress tests.

Capital Adequacy Target

Group policy, approved by the Board of Directors, which expresses its risk appetite, is to hold a level of capital adequacy higher than the threshold determined from time to time by the Bank of Israel, and higher than the rate required according to the results of the ICAAP. In addition, targets that the Group wishes to meet in the event of a stress scenario are defined.

Pursuant to a circular of the Supervisor of Banks dated 30 June 2010, the banks are subject to a core capital ratio of not less than 7.5%.

On 30 May 2013, the Supervisor of Banks issued final directives for the adoption of Basel III recommendations in Israel, including an amendment of Proper Conduct of Banking Business Regulation 201 regarding "Measurement and Capital Adequacy – Introduction, Incidence and Calculation of Requirements". Pursuant to this directive, all banking corporations will be required to comply with a minimum Tier 1 capital ratio of 9% with effect from 1 January 2015. In addition, a large banking corporation, whose total balance sheet assets on a consolidated basis constitutes at least 20% of the balance sheet assets in the banking system in Israel, will be required to comply with a minimum Tier 1 capital ratio of 10%, with effect from 1 January 2017. This additional provision applies to Leumi. Compliance with these targets will be achieved gradually. The Bank intends to maintain a planning margin above these targets.

In addition, all banking corporations in Israel will be required to maintain an overall capital ratio of 12.5% by 1 January 2015. A large banking corporation will be required to maintain an overall capital ratio of 13.5% by 1 January 2017.

For a possible effect on the capital ratio on the implementation of accounting standards regarding employee rights, see chapter, "Criteria Accounting Policy" below.

Following an analysis of the ICAAP risk map, the Board of Directors of the Bank decided to determine the Leumi Group's overall capital adequacy target to be not less than 13.5% over the long term.

The Bank is prepared to meet the expected requirements of the Supervisor of Banks as set forth in these regulations.

For further information regarding the Basel III directives, see the section, "Basel Directives and Preparation in Leumi" in the chapter, "Risk Exposure and Risk Management" below.

The above capital adequacy policy refers to future activities of the Bank, and is defined as "forward-looking information". For the meaning of this term, see the section, "Description of the Banking Corporation's Business and Forward-Looking Information", below.

Distribution of Dividends

During 2011-2013, the Bank did not distribute dividends.

a. The following table presents details of cash dividends declared and/or paid in the Group*:

**	**2013**	2012	2011
1. Bank Leumi le-Israel B.M. - in NIS millions**	**-**	-	-
2. The Arab Israel Bank Ltd. - in NIS millions	**80**	-	-
3. Leumi Card – in NIS millions	**30**	-	40.0
4. Leumi Private Bank – in CHF millions	**-**	-	70.0
5. Leumi Re – in US$ millions	**18**	-	-
6. Bank Leumi Luxinvest – in US$ millions	**-**	-	5.0
7. Other investments in the Group - in NIS millions	**24**	7.7	119.2
8. Israel Corporation Ltd. – in NIS millions	**-**	80.8	43.3

* The Group's share in the dividend, as set out in Note 6 to the Financial Statements, relates to the reporting year in respect of which the dividend was declared and not necessarily to the year of payment.

** The dividend for the fiscal year.

C. Other information

Principal Developments in the Economy(*)

General

In 2013, the Israeli economy grew at a rate of 3.3% in real terms, compared with a growth rate of 3.4% in 2012. The moderate growth stems principally from a slight increase of the export of goods (0.7%) and investments in fixed assets (1.7%).

The consumer price index rose by 1.8% in 2013, a rate which is in the price stability target centre of 1%-3%. During the past year, the Bank of Israel interest rates fell by a cumulative one percentage point, from 2.0% at the end of 2012 to 1.0% at the end of 2013. This came against a background of the low inflationary environment enabling support of growth in Israel, with an appreciation of the shekel also being a major factor in the interest decision. In the interest decision of March 2014, the interest rate was lowered to 0.75%, a level which was also retained in the interest decision for April 2014. The strengthening of the shekel against the dollar by some 7.0% and against the euro by some 2.8%, were affected, *inter alia*, by a combination of a surplus in the current account on the balance of payments and a substantial amount of capital foreign currency inflows.

The shares and convertible securities index rose during 2013 by some 15.3%, with the prices of corporate index-linked debentures increasing by some 9.5%, despite the moderate growth in the economy.

The global economy

In January 2014, the International Monetary Fund revised its estimate of the expected development of growth in the world for 2014. In most of the advanced countries, there was a slight upward change in the forecast, compared with that made in October 2013, while in the emerging and developing countries, there was no noticeable revision. In most countries, the rate of growth in 2014 was higher than that in 2013, in some cases, significantly higher. According to the Fund’s revised forecasts, growth in the United States and the Euro Area in 2014 will be some 2.8% and 1.0%, respectively, compared with 1.9% and (-0.4%), respectively, in 2013. In the Euro Area, there was a marked transition from recession to recovery, albeit with differences between the various countries.

The State Budget and its Financing

During 2013, the Government's budget deficit, excluding the provision of credit, amounted to some NIS 33.2 billion, about 3.15% of GDP. This is in comparison to the planned deficit of NIS 45.6 billion, about 4.33% of GDP. This gap derives from higher than forecast revenues amounting to NIS 5.7 billion, and lower than planned expenses, amounting to NIS 6.7 billion. The increase in tax revenues in excess of the forecast derives, *inter alia*, from revenues of a non-recurring nature (resulting from the sales of companies). With regard to total expenditure, it should be borne in mind that, from the beginning of the year until the end of July 2013, the Government operated without an approved budget framework.

On 14 May 2013, the government approved the economic program (the State Budget and the Arrangements Law) for 2013-2014. The Arrangements Law was approved by the Knesset on 29 July 2013 and, on 30 July 2013, the State budget was approved.

Foreign Trade and Capital Movements

Israel’s aggregate trade deficit in 2013 amounted to some US$ 14.3 billion, a decrease of some 22% (US$ 4 billion) compared with the deficit in 2012. The fall in the trade deficit is mostly due to a reduction in imports, compared to a moderate increase in exports. However, in shekel terms, there was a contraction in both imports and exports, as a result of the effect of the appreciation of the shekel exchange rate against the dollar and against the other major currencies. A large part of the reduction in imports stemmed from the reduction in value of the imports of energy products into Israel amounting to US$ 1.5 billion as a result of the effect of commencing gas production in the second quarter of the year.

(*) Source of data: publications of the Central Bureau of Statistics, the Bank of Israel, the Ministry of Finance and the Tel Aviv Stock Exchange.

Foreign currency capital transactions were characterized in 2013 by a higher total of capital outflows compared with capital inflows. Direct investments in Israel, via the banking system, amounted to some US$ 8.8 billion during the said period, while financial investments amounted to US$ 1.5 billion. In comparison, the volume of investments of Israeli residents abroad (direct investments through banks in Israel and financial investments) amounted to US$ 11.7 billion, mostly financial investments. During the period, the institutional investors reduced their exposure to foreign currency by expanding the currency hedging and so contributed to the strengthening of the shekel.

Exchange Rates and Foreign Currency Reserves

In 2013, there was an appreciation of some 7.0% in the rate of the shekel against the dollar, while the shekel appreciated more moderately by 2.8%. This appreciation was affected by the healthy state of Israel's foreign currency accounts (particularly, the surplus in the current account on the balance of payments) and the substantial increase in foreign currency capital inflows, mainly as a result of an increase in foreign direct investments (FDI).

On 13 May 2013, the Bank of Israel announced a program of foreign currency purchases which will offset the effect of gas production on the exchange rate. The amounts to be purchased as part of this program will be added to the Bank of Israel's foreign currency balances, but will be managed separately with a longer term horizon. This program will be re-examined when the "Wealth Fund" is put into operation, which is expected to be during 2018. On 2 October 2013, the central bank announced that, in 2014, it intends to purchase US$ 3.5 billion for this purpose.

Foreign currency balances at the Bank of Israel at the end of December 2013 stood at US$ 81.8 billion, compared with US$ 75.9 billion at the end of December 2012.

Against the background of the appreciation of the shekel and the plan to purchase foreign currency, which was decided on 13 May, the Bank of Israel purchased US$ 3.2 billion, plus US$ 2.1 billion as part of the program to offset the effect of gas production on the exchange rate. In January 2014, the Bank of Israel increased the purchases of foreign currency which amounted to US$ 1.73 billion, of which US$ 0.23 billion is within the framework of a program of purchases to offset the effect of gas production on the rate of exchange.

Inflation and Monetary Policy

During 2013, the Israeli consumer price index increased by some 1.8%, a rate which is within the range the Government's price stability target of between 1% and 3%. The largest contribution to the increase in the index in the past year was in the housing sector, which increased by some 2.9% and the food sector which increased by some 3.3%. These items and others, were affected, *inter alia*, by the increase in indirect taxes. During the year, VAT, in particular, rose by one percent. One item which notably fell was telephone and cellular services, which dropped by 10.1%, due to the effect of the reduction in the prices of cellular services.

Bank of Israel interest rates, which stood in December 2012 at 2.0%, fell several times during 2013, and in October 2013, stood at 1.0%. The reasons for the reduction in interest rates were the need to lend additional support to economic activity, against a backdrop of the downward revision of the global growth forecasts and the appreciation of the shekel, while, on the other hand, there were inflationary pressures. In the interest rate decision for February 2014, the interest rate was retained at a level of 1.0%, while in the interest decision of March 2014, it was lowered by 0.25 percentage points to 0.75%.

Capital Market

The shares and convertible securities index rose by some 15.3% in 2013, following an increase of some 4.5% in 2012. Increases in the rates were affected by the low level of Bank of Israel interest, the geopolitical situation in the region and increases in stock exchanges worldwide, particularly in the United States.

Average daily trading volumes of shares and convertible securities increased in 2013 by some 8.8%, compared to the average for 2012, and amounted to some NIS 1,172 million. In the fourth quarter of the year, volumes increased compared to the first three quarters of the year.

The government bond market in the past year was characterized by a trend of moderate price increases. The price of index-linked government bond increased by some 3.0%, while unlinked debentures increased by 4.0% (the fixed interest (*Shahar*) bond indices rose by some 4.4% and the variable interest (*Gilon*) bond index increased by some 2.3%).

In the index-linked non-government debenture market (corporate bonds) in 2013, there were price increases of some 9.5%. The increases occurred despite the slowdown in activity in the business sector.

Financial Assets held by the Public

The value of the portfolio of financial assets held by the public increased in 2013 by some 8.6% resulting in some NIS 2,958 billion at the end of December 2013. This increase in the value of the portfolio derived from an increase in all its components. The weight of shares (in Israel and abroad) in the financial assets portfolio of the Israeli public reached some 24.7% at the end of December 2013, compared to 21.7% at the end of December 2012. Most of the increase derived from a significant increase in the balance of shares in Israel and abroad.

Bank Credit

Bank credit in the economy granted to the private sector, including corporate credit and household credit, (before allowances for credit losses) increased in 2013 by a moderate rate of some 2.3%. This was a consequence of an increase in credit extended to the household sector. Housing credit, in particular, increased by some 9.1%, while non-housing credit (consumer credit) increased by some 6.8%. In contrast, there was a decrease of 2.8% in credit allocated to the business sector, which is the major component of the credit extended to the private sector.

The table below shows Israel's and the Bank's credit ratings in 13 March 2014:

	Rating agency	Short-term rating	Long-term rating	Long-term rating outlook
State of Israel’s rating in foreign currency	Moody’s	P-1	A1	stable
	S&P	A-1	A+	stable
	Fitch	F1	A	stable
Leumi’s rating in foreign currency	Moody’s	P-1	A2	stable
	S&P	A-2	BBB+	stable
	Fitch	F2	A-	stable
Leumi’s rating in local currency for debentures and standard deposits	Ma'alot	-	AA+	stable
	Midroog	P-1	Aaa	stable
Leumi’s rating in local currency for subordinated capital notes	Ma’alot	-	AA	stable
	Midroog	-	Aa1	negative
Leumi’s rating in local currency for subordinated capital notes (Upper Tier II)	Ma’alot	-	(A, AA-)*	stable
	Midroog	-	Aa2	negative

* A: Upper Tier II capital with compulsory conversion into shares of the principal.
AA-: "New" Upper Tier II capital, not convertible into shares.

Developments in Leumi Share Price

In 2013, the price of Leumi shares rose from 1,267 points to 1,418 points, a change of 11.9%. During this period, the Bank’s market value rose from NIS 18.7 billion to NIS 20.9 billion.

The following table sets out details of changes in representative exchange rates and the CPI and the rates of change therein:

	December 31				
	2013	2012	2011	2010	2009
	NIS				
Exchange rate:					
U.S. dollar	**3.471**	3.733	3.821	3.549	3.775
Euro	**4.782**	4.921	4.938	4.738	5.442
Pound sterling	**5.742**	6.037	5.892	5.493	6.111
Swiss franc	**3.897**	4.077	4.062	3.788	3.667
Consumer price index:	(points)				
For November (the "known" index)	**107.5**	105.5	104.0	101.4	99.1
Index for December	**107.6**	105.7	104.0	101.8	99.1

Rates of change were as follows:

	December 31				
	2013	2012	2011	2010	2009
	in %				
Rate of change:					
U.S. dollar	**(7.0)**	(2.3)	7.7	(6.0)	(0.7)
Euro	**(2.8)**	(0.3)	4.2	(12.9)	2.7
Pound sterling	**(4.9)**	2.5	7.3	(10.1)	10.2
Swiss franc	**(4.4)**	0.4	7.2	3.3	2.9
Consumer price index:					
For November (the "known" index)	**1.9**	1.4	2.6	2.3	3.8
Index for December	**1.8**	1.6	2.2	2.7	3.9

Regulation, General Environment and the Effect of External Factors on Activities

Part of the information in this Section is "forward-looking information". For the meaning of this term, see the section, "Description of the Banking Corporation's Business and Forward-Looking Information in the Directors' Report" below.

Legislation and Regulation affecting the Banking System

Promotion of Competition and Reduction of Concentration, 2013

On 11 December 2013, the Promotion of Competition and Reduction of Concentration Law, 2013, was published.

The main points are:

- The law requires the relevant regulatory authorities to weigh considerations of market-wide concentration and to consult with the Concentration Reduction Committee on the following subjects: the allocation of rights to concentration factors with the allocation of rights being defined as the grant of a license or engagement in a contract in the area of essential infrastructure (including, under certain condition, their renewal or extension), the grant of approval required for the transfer of a license or contract as aforesaid, or for the transfer of the means of control (above a certain rate) in the holder of a license or contract, as aforesaid, the transfer of the means of control (above a certain rate) held by the State and the grant of the State's approval for the transfer of the means of control (above a certain rate) in a corporation which was subject to the provisions of the Government Corporations Law.

- The law requires the relevant regulatory authorities to weigh considerations of the promotion of industry competition and to consult with the Antitrust Commission in the allocation of a right which is likely to have an impact on competition, both with regard to a right in an area of essential infrastructure, and with regard to a right in the area of activity which is not an area of essential infrastructure, providing that the number of workers in the relevant industry in which the right is allocated is limited.

- The law prohibits the control in companies in a pyramidal structure including more than two layers of companies which are reported corporations ("layer company") and provides transitional provisions in relation to an existing pyramidal structure at the publication date of the law. Until the end of a four-year period from the date the law is published, the law permits control in a fourth layer and above company, and until the end of a six-year period from the date the law is published, the law permits control in a third layer company. In addition, strengthened rules of corporate governance with regard to third layer and above companies in the transitional period which commenced six months from the date the law is published and ends four or six years after the law is published, whichever is the case.

- The law authorizes the Finance Minister and the Governor of the Bank of Israel (or whoever they authorize) to determine, within a year of the publication of the law, restrictions on credit granted to a corporation or to a business group by financial entities in aggregate, taking into account the indebtedness of each corporation or the total indebtedness of the business group. At this stage, the aforesaid restrictions have not been formulated. Pursuant to the law, the Minister of Finance and the Governor of the Bank of Israel are entitled to determine that the aforesaid restrictions, when determined, will also apply to borrower groups and related companies in which conditions as will be provided are fulfilled.

- The law requires a separation between significant non-bank corporations and significant financial entities and provides restrictions on the holding of a significant financial entity and a significant non-bank corporation in the hands of the same controlling shareholder, restrictions on the holding of a non-bank corporation in a significant financial entity, restrictions on the holding of a banking corporation in a significant non-bank corporation and in an insurer which is a significant financial entity, as detailed below, a prohibition on the controlling owner in a banking corporation which is a significant financial entity to control an insurer which is a significant financial entity and restrictions on the holding of an insurer, a managing company and a fund manager in significant non-bank corporations.

- The law amended, *inter alia*, section 24a of the Banking Law (Licensing), 1981, ("the Banking Law"), such that instead of restrictions on the holdings of a banking corporation in non-bank holding corporations, it is provided that a banking corporation will be entitled to hold only up to 1% of the means of control of significant non-bank corporation, as defined in the Banking Law, or of an insurer which is a significant financial entity, as defined there. However, a banking corporation is entitled to hold up to 10% of the means of control of one significant non-bank corporation and one insurer which is a significant financial entity. A banking corporation which holds, prior to the publication of the law (11 December 2013), the means of control in significant banking corporations or significant insurers, as applicable, at a rate exceeding the permitted limit as mentioned above, is entitled to continue to hold those means of control for six years from the publication date of the law, i.e., 11 December 2019.

  The Bank holds 17.96% of the means of control in the Israel Corporation Ltd., which is considered a significant non-bank corporation pursuant to the Banking Law, and accordingly, the Bank is obliged to reduce its holdings in the Israel Corporation to a rate of 10% by 11 December 2019.

Sales Law (Apartments) (Guarantee of Investments of Apartment Purchasers) (Amendment no. 7) (Notice Regarding the Deletion of Registration of a Lien), 2013

The law was published on 3 December 2013. The law regulates the issue of a contingent exception letter by the banking corporation which is granting financial support for construction, or a banking corporation which is extending sale guarantees to purchasers in favor of purchasers of apartments.

The law also applies to an insurer that issues insurance policies in favor of apartment purchasers.

The wording of the contingent exception letter will be consistent with the wording appearing in the addendum to the law. The letter sets out the conditions, in compliance with which the bank undertakes not to exercise the lien in its favor on the apartment, and also a subsequent undertaking that the bank will take steps to delete any registration of the lien on the apartment within a reasonable time after the apartment is registered as a separate registration unit. The law is effective 30 days after its publication date.

Securities Law (Amendment no. 53) (Electronic Voting System), 2013

On 31 October 2013, Amendment no. 53 to the Securities Law was published in *Reshumot* which (inter alia) regulates the issue of the electronic voting system. The amendment is intended to establish the legal infrastructure for the Israel Securities Authority to set up an electronic voting system. This system will enable shareholders and holders of liability notes and options to exercise their voting rights, without the need to obtain from a stock exchange member confirmation of ownership of the security.

For the purpose of its activation, the electronic voting system will require an interface with stock exchange members for receiving the data of holders of securities who are eligible to vote in a specific meeting. In addition, stock exchange members will be required to supply potential voters with the information and details they need in order to vote, including information regarding the relevant meeting and identification codes for voting using the system.

In accordance with the proposed law amending the Partnerships Order (no. 5) (Corporate Governance in a Limited Public Partnership), 2014, holders of participation units in traded partnerships will also be able to vote using the electronic voting system.

Law for Reliefs in the Capital Market and Encouragement of Activities therein (Legislative Amendments), 2014

On 27 January 2014, the Law for Reliefs in the Capital Market and Encouragement of Activities therein (Legislative Amendments), 2014 was published in *Reshumot*. Pursuant to the law, the Law for the Regulation of Engagement in Investment Consulting, Investment Marketing and Investment Portfolio Management, 1995 and the Joint Trust Investment Law, 1994, were amended, in order to create a legal framework for the deposit and loans fund (hereinafter, "Kapam") – a new product, which will constitute a sub-type of monetary shekel mutual fund.

The aim of the Kapam is to be an effective substitute for the bank deposit. Its features are: (a) a solid product – the assets to be held in the fund will be solely bank deposits and short-term loans whose term to redemption does not exceed one year, (b) characteristics of the data related to the product – the data of the "Kapam" will also include an indication regarding "an estimate of the annual yield" inherent in the assets of the fund, and thus will enable anyone wishing to invest in it to assess the advisability of an investment therein compared with the banking alternative, (c) design and positioning of the product – one that behaves in a uniform, simple and very conservative manner, (d) the exclusion of the "Kapam" from the definition of a "financial asset" in the Consulting Law – the product will also be able to be sold to the public through a mediator who does not hold a consultant's license, i.e., by an investment clerk in the bank who is designated to become the main distribution channel for the product.

In addition, the law deals with the following areas: the grant of an exemption to banks from the requirement to place a sign on the subject of marketing investments; customer requirements will be updated at a frequency to be determined by the Israeli Securities Authority instead of once a year; the prohibition regarding the receipt of benefits in respect of preparing analyses will not apply in cases and circumstances to be determined by the Israel Securities Authority; the Bank will report to the Israel Securities Authority without delay on the joining of a license holder and the termination of his employment. In addition, the Bank will report to the Israel Securities Authority on the position of the license holder once a year, instead of once a quarter, as it is now; the consent of the Minister of Finance (at the proposal of the Israel Securities Authority or after consulting with it, and with the approval of the Knesset Finance Committee) to determine conditions for extending the period of a shelf prospectus by 12 months; the consent of the Israel Securities Authority to determine cases in which the publication of a shelf proposal is subject to the receipt of a permit from the Israel Securities Authority; the establishment of a ceiling as to the amount of the monetary sanction in respect of a continuing breach.

Banking Rules (Service to the Customer) (Commissions), 2008

On 1 August 2013, Amendment no. 2 of the Banking Rules (Service to the Customer) (Commissions), 2008 ("the Commission Rules"), came into force. Pursuant to the amendment, the annual business turnover ceiling of a "small business" in the retail list of charges was changed from NIS 1 million to NIS 5 million.

In addition, it was provided that an individual who is a business will be classified as a "small business", providing the banking corporation has not found that the business turnover of that individual in the past year exceeds NIS 5 million. If the banking corporation has reasonable grounds for assuming that the business turnover of the said individual in the past year exceeds NIS 5 million, it is entitled to request that individual in writing to furnish it with an annual report. If this request is not addressed, the banking corporation is entitled to classify the individual as a business which is not a small business, with effect from the first of the month following the month after sending the request.
The bank will notify the corporations in writing of the fact that if they furnish the bank with an "annual report" as defined in the commission rules, according to which their annual business turnover does not exceed NIS 5 million per annum, the bank will take steps to classify their account as a "small business". The classification is in force for a year and its renewal is conditional on furnishing up-to-date documents.

On 8 October 2013, the Banking Supervision Department published a further amendment to the Commission Rules, which will come into force on 1 April 2014. Pursuant to the amendment, banks are obliged to offer individual customers and small businesses various paths for the payment of current account commissions - Part 1 in the charge-list ("current account"), as follows:

"Basic path" – a path which includes up to one transaction by bank clerk and up to 10 transactions by direct channel, in the course of a month;

"Extended path" – a path which includes up to 10 transactions by bank clerk and up to 50 transactions by direct channel, and all in the course of a one-month period;

"Extended Plus path" – a path which includes the transactions and their number according to the extended channel, and also other services according to the decision of the banking corporation, and all in the course of a one-month period;

A banking corporation should include, as part of the services offered to its customers, the basic path and the extended path and should enable every customer to join them. As regards the Extended Plus path – there is no obligation to offer it.

A customer is entitled to join one of the paths by giving notice to the banking corporation in writing or in a recorded conversation, or in a computerized telephone reply. If a customer joins one of the paths, and exceeds the maximum quota of transactions included therein, the banking corporation is entitled to charge a commission for the additional transactions according to the full list of tariffs as defined in the Commission Rules.

On 5 March 2014, the Bank of Israel published a draft of the Banking Order (Service to the Customer) (Supervision of Basic Path Service), 2014, which provides that the "Basic path" is a regulated service, with a maximum price of NIS 10.

Proposed Law to Amend the Banking Law (Service to the Customer) (Amendment no. 19), 2012

On 10 March 2014, Amendment no. 19 to the Banking Law (Service to the Customer) was published. Pursuant to the law, a banking corporation may not make a loan available for immediate repayment and will not take legal proceedings against a customer due to failure to comply with the terms of a loan, including failure to repay the loan in whole or in part ("action regarding the loan"), unless it has furnished the customer with a written notice, 21 working days before taking the action regarding the loan in a way that the banking corporation takes to furnish notices to that customer, and by personal delivery to the customer's address registered with the banking corporation. The said notice must include various details as set forth in the proposed law. However, a banking corporation will not be obliged to furnish a notice as aforesaid if its delivery raises a tangible concern of impairment in the banking corporation's ability to collect due to an adverse change in the customer's repayment capacity or because of other conditions which require immediate performance of an action regarding the loan.

The proposed arrangement will commence six months after the publication date of the law in *Reshumot* and it will also apply to loans made by the banking corporation before its inception.

Draft Amendment of the Joint Trust Investments Regulations (Distribution Commission) (Amendment no. 15), 2013

The draft was published on the website of the Israel Securities Authority for comments from the public in November 2013, in anticipation of the implementation of Amendment no. 15 to the Joint Trust Investments Law, which is due to regulate the distribution of the foreign funds in Israel.

According to the current situation, distribution commission regulations permit a distributor to collect, in addition to a distribution commission which is collected from the fund managers, also commissions from the customers in respect of purchase, sale, redemption or holding of funds. Pursuant to the amendment, it is proposed to cancel the said right, and in lieu thereof, to establish an across-the-board prohibition on the collection of the aforesaid commissions, where a distribution commission is paid by virtue of distribution agreement signed with the fund manager, unless a permit as aforesaid has been determined within the framework of an explicit determination.

Draft Banking Rules (Service to the Customer) (Fair Disclosure and Delivery of Documents) (Amendment), 2013

According to the draft amendment, a banking corporation is obliged to furnish any person asking to open an account for the purpose of a business with an explanatory page, clarifying, in a separate document, the practical significance of the classification of the account as a "small business" as defined in the Banking Rules (Service to the Customer) (Commissions), for the purpose of the service charge-list.

In addition, pursuant to the amendment, a banking corporation is obliged to furnish a customer requesting to join a path, as defined in the Banking Rules (Service to the Customer) (Commissions), prior to his joining, written information summarizing the amounts of the commissions collected from him during the quarter prior to the submission of the joining request, for the services included in that path, including a minimum acceptance commission, if any, according to the summary of the types of transaction carried out and their number divided into months. The Supervisor is entitled to make various stipulations regarding the information to be furnished to the customer as aforesaid.

Legislation and regulation in pension consulting

On 22 July 2013 the Supervisor of the Capital Market, Insurance and Saving Division in the Ministry of Finance ("the Supervisor") published an updated version of a circular regarding "the power of attorney to a license-holder", in light of update proposals that arose during preparations to implement the circular. On 7 October 2013, the Supervisor published a notice according to which the revised "power of attorney to a license-holder" circular would be deferred to 30 November 2013.

As a part of the preparations for working with the central pension clearing system (hereinafter "the system"), on 22 July 2013, the Supervisor published an updated version of a circular regarding "the obligation of using a central pension clearing system", and a circular regarding "the identification of users and management of authorizations for using a central pension clearing system", which regulates the granting of authorities to view data in the system. On 7 October 2013, the Supervisor published a notice, according to which it was decided that the obligation of using the system to obtain one-time information would come into force on 30 November 2013.

On 6 August 2013, a draft circular was published on the supply of back-office operating services and front-office operating services, which was intended to regulate the supply of services to an institutional body by a banking corporation. On 19 December 2013, the Supervisor announced that it had been decided to extend the interim period as aforesaid in the circular for agents and advisors, "Agreements for the Provision of Services – Second Update", to 30 June 2014.

Directives of the Supervisor of Banks

Proper Conduct of Banking Business Management Regulation no. 301A on Remuneration Policy

On 19 November 2013, a new Proper Conduct of Banking Business Management Regulation was published regarding remuneration in a banking corporation (Regulation 301A) ("the directive"). The object of the directive is to establish principles, intended to ensure that the remuneration arrangements in banking corporations in Israel are consistent with the risk management structure and long-term objects of the banking corporation. According to the directive, adequate remuneration arrangements include appropriate corporate governance principles which banking corporations are obliged to adopt, principles which assist in achieving and maintaining public confidence in the banking system.

According to the directive, every banking corporation must adopt a remuneration policy that will apply to all employees of the banking corporation and will relate to all types of remuneration. The remuneration policy will promote established and effective risk management and will not encourage the taking of risks beyond the banking corporation's risk appetite.

A banking corporation will also have to specify the "principal employees" in the banking corporation, who are the officers in the corporation, and also the employees whose activity is likely to have a significant influence on the banking corporation's risk profile.

The directive contains requirements that will apply to all employees of the banking corporation, requirements that will apply to the "principal employees" in the banking corporation, and requirements that will apply only to officers in the banking corporation.

The remuneration to the principal employees (including the officeholders) will be adjusted for all the risks and will be taken into account in the cost and amount of capital which is required to support the risks to which the banking corporation is exposed and in the cost and risk of the liquidity. The variable remuneration to the principal employees must be dependent on fulfilling the predetermined criteria, and based on a combination of the employee, the business unit and the entire banking corporation. The payment of the remuneration must be subject to deferral arrangements (more than half of the variable remuneration will be deferred over a number of years) and contingent on financial and other achievements over a period. The draft directive further provides that the fixed remuneration to the principal employees must by a significant part of the total remuneration, with the maximum variable remuneration (including remuneration in respect of the termination of employment which is classified as variable remuneration) not to exceed 100% of the fixed remuneration for each employee, except in exceptional cases, and subject to the requirements of the directive, in which the banking corporation will be entitled to determined that the maximum variable remuneration will reach 200% of the fixed remuneration. The draft of the directive further clarifies that the classification of the remuneration as fixed or variable will not be affected by the means of paying the remuneration (cash, shares, etc.), but in order for the remuneration to be classified as "fixed remuneration", it is necessary for its monetary amount to be fixed and not restricted as to use on its date of grant.

The directive provides control, documentation and audit regulations in connection with the remuneration policy, arrangements and mechanisms in the banking corporation, as well as regulations for remuneration of the risk management audit and control functions.

The directive also provides that at least 50% of the total variable remuneration granted in respect of a calendar year to an officer, as defined in the Companies Law, be granted in the form of shares and share-based instruments, the entitlement to which vests over a number of years, in accordance with performance in this period.

In addition, the directive provides that a grant that is contingent only on the completion of a predetermined period of employment, which is intended to guarantee the continuation of employment, is variable remuneration which is not contingent on performance, and therefore, does not form part of the remuneration program of a banking corporation.

The directive further provides that remuneration granted to a principal employee in respect of the termination of employment, beyond that provided in the employment terms of all of the employees of the banking corporation, should be classified as variable remuneration, and therefore, will take into account actual performance over time and the reason for terminating employment and will be subject to arrangements for the deferral of payments according to period.

In addition, the transitional provisions of the directive are as follows: (a) by no later than 30 June 2014, a banking corporation must determine a remuneration policy which corresponds to that provided in the directive; (b) the requirements provided in the directive will apply to any individual remuneration agreement of the banking corporation with a principal employee, which must be approved by the banking corporation from the publication date of the directive (19 November 2013) and thereafter; (c) the requirements provided in the directive will apply to individual remuneration agreements as stated above that are approved from 3 June 2013 and thereafter, no later than 30 June 2014; and (d) The requirements provided in the directive will apply to individual remuneration agreements as stated above before 3 June 2013, no later than 31 December 2016.

For details regarding the remuneration policy in the Bank, see note 15 to the financial statements, below.

Amendment to Proper Conduct of Banking Business Regulation no. 301 - Board of Directors

On 25 December 2013, an amendment to Proper Conduct of Banking Business Regulation no. 301- "Board of Directors" was published.

Pursuant to the amendment to the directive, the definition of a "banking corporation" was expanded, such that the directive will also apply formally to clearinghouses and banking corporations which are joint services companies. Also in the regulation, the authority of the Supervisor of Banks to change or exempt a banking corporation or director from certain provisions in the directive was expanded.

The amendment provides regulations regarding the prohibition on the cross-tenure of office of a director in a banking corporation and at the same time as a director, member of an investment committee, member of a credit committee, or employee ("office-holder" for the purpose of this section) in a financial entity or in a corporation which controls a financial entity. An exception to this case is when a director in a large banking corporation is entitled to serve in both a small financial entity, or in a corporation which controls a small financial entity, and can serve in a number of small financial entities in the same financial group, providing that the total assets of the aforesaid small entities do not together exceed NIS 2 billion, and vice versa. It further provides that, in one banking group, no more than two directors will serve who are, at the same time, serving in financial entities (included in Appendix C to the Directive) and who belong to the same financial group.

In addition, in the amended directive the restriction which was established that an external director cannot serve as chairman of the board of directors was curtailed, such that the restriction will only apply to a banking corporation with a controlling core, i.e., an external director in a banking corporation without a controlling core may serve as a chairman of a board of directors.

In addition to the prohibition on the appointment of a substitute director in a board of directors of a banking corporation, a prohibition was added on the appointment of an observer who will participate in the discussions of the board of directors, including in the discussions of its committees. However, a director is entitled to participate in the meeting of a committee of the board of directors in which he is not a member, providing that his participation is not permanent.

Proper Conduct of Banking Management Regulation no. 421 regarding a decrease or increase in interest rates

On 9 September 2013, the Banking Supervision Department published Proper Conduct of Banking Management Regulation no. 421, which deals with the reduction or increase in interest rates. Pursuant to the directive, in loans for an "individual" and a "small business" in which the rate of interest is not fixed and is not known throughout the period of the loan, and in loans made in parts, on the dates of changing the interest on the loan, the reduction or increase in the basic interest rate which applied at the date of making the loan will apply. A special mechanism was determined for loans in which the basic interest rate is LIBOR. The directive refers to all types of loans, including housing loans, credit facilities in an account and credit facilities in debit cards.

In addition, it was provided that in deposits of an "individual" or of a "small business" in which the interest rate is not fixed and is not known throughout the whole period, and in renewable deposits, at the date of a change in interest or renewal of the deposit, the reduction or increase in the basic interest rate which applied at the date of making the deposit will apply. The obligation does not apply in the case where the customer withdraws part of the deposit amount during the deposit period or at the date of renewal. This directive will come into force from 1 January 2014, with the exception of paragraph 2, which deals with deposits, which comes into force on 1 July 2014.

Amendment of Proper Conduct of Banking Management Regulation no. 451 - Procedures for Granting Housing Loans

On 1 May 2013, the Banking Supervision Department published an amendment to Proper Conduct of Banking Management Regulation no. 451, pursuant to which the information that banks are obliged to furnish to those taking housing loans has been expanded with regard to their rights, should they encounter a situation of arrears in the repayment of the loan. In accordance with the amendment, the banks are obliged to furnish a borrower, who is in arrears in payments, with detailed information regarding his right to apply to a "special committee" which was established by virtue of the Housing Loans Law, 1992, which was intended to alleviate the repayment of loan installments due to the economic situation of the borrower. It was also established that a bank is obliged to furnish the borrower who is in arrears with detailed information regarding the ways of communicating with the relevant factors in the bank. In addition, it is provided that the bank is obliged to take appropriate steps in order to be made aware of any request by the borrower to regulate the debt in arrears, even if this is done via a representative, in order that he will be able to examine the borrower's request in its own right. It is further provided that the banks should make the borrower aware regarding their obligation to update the license holders operating pursuant to the Credit Data Service Law. The amendment came into force on 1 August 2013.

Changes in the presentation of the commissions list of tariffs in the bank's website:

On 22 October 2013, the Supervisor of Banks published a letter, dictating changes in the method of presentation of the commission charge-list in the bank's Internet website.

The letter required a customer to be able to do the following:

a. Access the list of tariffs from a prominent place in the site, through an unambiguous link and not via an icon.

b. To download the list of tariffs in an Excel or PDF format.

c. Access to the list of tariffs via a search engine according to a key word "tariff" or "commissions".

d. Presentation of charge-lists at the level of each chapter and by folder.

The provisions of the letter came into force on 1 January 2014.

Bringing forward the date of publication of financial statements to the public

On 29 September 2013, the Banking Supervision Department published a directive according to which any banking corporation must publish the annual financial statements within two months of the year-end (by the end of February) and not within three months, as the regulations currently require. At the same time, the date for reporting the quarterly financial statements is shortened from two months to 45 days from the end of the quarter.

The bringing forward of the publication dates is intended to correspond with generally accepted practice in the United States, *mutatis mutandis*, and in order to improve the availability of the information to financial statements readers.

The change will be implemented gradually, over three years, until its full application in 2016.

The Bank, with the consent of the Banking Supervision Department, has deferred the implementation of the directive regarding the bringing forward of the publication date of the financial statements, such that this directive will be applied for the first time only in the financial statements for the first quarter of 2014.

The implementation of the directive requires a change in the method recording the equity profits of a company included on equity basis, thus, from the first quarter of 2014, there will be continual gap of a quarter between the reporting date of the Bank and that of the company included on equity basis. See below in the in the financial statements, note 1 – Significant accounting policies.

Restrictions on the grant of housing loans

On 29 August 2013, the Banking Supervision Department published directives on restrictions on the grant of housing loans. The restrictions limit the rate of repayment from income, the portion of the loan that is granted with variable interest and the final period for repaying the loan. The object of the directives is to mitigate the risk, particularly, the interest risk, of the public who take mortgages on terms that are liable to endanger its future ability to repay the mortgage, and, as a consequence, the risk inherent in these loans for the banking system.

The main points of the directives are as follows:

a. A banking corporation may not approve and may not make a housing loan at a monthly rate of repayment exceeding 50% of the income of the borrower. In housing loans, where the rate of repayment out of income exceeds 40%, a risk weight of 100% should be allocated to the loan for calculating the capital adequacy ratio.

b. A banking corporation may approve and make a housing loan only when the following two conditions are fulfilled:

1. The ratio of the portion of the housing loan at variable interest to the total amount of the loan does not exceed 66.66%

2. The ratio of the portion of the loan at variable interest rate bearing interest that is liable to change during a period of less than five years from the date of approving a loan and the total loan does not exceed.33.33%.

c. A banking corporation may not approve or grant a housing loan for a final repayment period exceeding 30 years.

A banking corporation may not approve or refinance a housing loan, if, as a result of the refinancing, one of the restrictions mentioned above is exceeded, or an exception which existed prior to the refinancing was increased.

These directives will apply to housing loans for which agreement in principle was granted since 1 September 2013.

Draft Proper Conduct of Banking Management Directive regarding Annual Report to Banking Corporation customers

On 31 October 2013, the Banking Supervision Department distributed to the members of the Bank-Customer Committee a preliminary version of a draft Proper Conduct of Banking Management directive, "Annual Report to Customers of Banking Corporations".

The directive regulates the banking corporation's duty of reporting to its customers on all of the customer's assets and liabilities in the banking corporation, including the total income and expenses during a year, in respect of assets, liabilities and routine activity in the account.

Pursuant to the directive, the annual report is intended to improve the ability of the customers to monitor their activity in the account, and increase their ability to compare various banking products and services.

The periodic report is intended to provide the customer with information regarding his credit rating, as determined in the banking corporation's rating model, so that potential lenders can assess the customer's financial position.

The directive deals with the furnishing of two reports to the customer – one, in a shortened format and other, more detailed, and includes guidelines relating to the information channels through which the information is made available to the customer.

Draft Proper Conduct of Banking Management Directive no. 414 – Disclosure of the Cost of Services in Securities

On 16 October 2013, the Banking Supervision Department published a draft Proper Conduct of Banking Management Directive dealing with the disclosure of the cost of services in securities, whereby the banking corporations will be required to provide customers who make transactions of sale and purchase or redemption of Israeli and/or foreign securities with comparative information regarding commissions paid by customers who have made similar transactions to that made by that customer.

International Regulations

Foreign Account Tax Compliance Act – FATCA

In March 2010, the Internal Revenue Code in the United States (the U.S. Income Tax Law) was amended such that it brings into effect a reporting regime which aims to compel foreign financial institutions (FFI) to transfer information regarding accounts held by U.S. customers. Thus, the law considerably expands the disclosure and reporting requirements imposed on FFI in relation to U.S. accounts. In January 2013, regulations were published by the United States Internal Revenue Service ("IRS"), (which were amended in September 2013, and February 2014), providing operative directives for implementing the law. In July 2013, the U.S. authorities announced a six-month deferral of the effective date of the requirements of the law to 1 July 2014. Pursuant to the law and regulations, an FFI is obliged to enter into an agreement with the IRS, whereby it will undertake, *inter alia*, to locate U.S. accounts, report on them to the IRS and deduct tax from customers who refuse to furnish the required information and documents. An FFI that does not sign an agreement with the IRS will be charged a deduction of tax in respect of income from U.S. sources.

In order to be prepared for the implementation of the law in Leumi Group, the Bank has set up a steering committee which is studying and monitoring developments in the law and regulations. Under its guidance, the Bank is taking steps to implement working procedures which have been characterized and to develop a system for complying with the FATCA requirements according to the work program established. In addition, the Bank has carried out a demarcation of the project and an examination of the Group companies relevant to FATCA, and a work program has been established which is being applied by them. In recent years, working procedures for dealing with U.S, customers have been established in the Bank and in the subsidiaries. In September 2011, a letter was sent to managers regarding the Bank's policies with regard to FATCA, reiterating and emphasizing the Bank's policy of not advising customers on taxation matters, particularly U.S. tax, and not assisting them in concealing their identity, and since then, additional procedures were issued regulating the area of identifying, locating and handling U.S. customers, as a complement to the procedures previously issued.

The IRS has published a model of a trans-national agreement for the implementation of the FATCA regulations and issued other notices regarding special agreements for implementing the FATCA between the United States and the United Kingdom, Switzerland, and several other countries. Financial institutions and their customers located in a country, which is a signatory to the trans-national agreement for implementation of FATCA regulations, will enjoy certain reliefs within the framework of the FATCA requirements.

In August 2012, the Finance Ministry announced the setting up of a team headed by the Commissioner of State Revenue, to examine the implementation of the FATCA regulations in Israel, "including examining the possibility of implementing a bilateral agreement between the State of Israel and the United States, which is intended to give relief to the financial entities with regard to implementation". According to the announcement, the team includes representatives of the Finance Ministry, the Bank of Israel, the Securities Authority and the Justice Ministry.

In March 2014, the Bank of Israel published a draft directive draft for banking corporations to be prepared for the application of the FATCA, whether by 1 July 2014, an inter-government agreement for the implementation of the FATCA is signed or not. In particular, the banking corporations have been instructed in the following subjects: corporate governance procedures (appointment of responsible official, establishment of working team, determination of policies and procedures, reports to the management and the board of directors), examination of the need to register and sign an agreement with the U.S. authorities in accordance with the timetables set forth in the directives, and conduct with customers, in particular, the option of refusing to render banking services to a customer who does not cooperate with the banking corporation in the way required for implementation of the directives.

On 13 March 2014, the Ministerial Committee for Social and Economic Affairs (the Socioeconomic Cabinet) resolved to instruct the Finance Minister to advance the negotiation regarding the bilateral agreement between Israel and the United States as noted above, to direct him to submit an alternative law for implementing the said agreement and to issue to the public information on the agreement which is formulated.

Due to the lack of clarity with regard to the date of signing the bilateral agreement, Bank Leumi is prepared for implementation of the FATCA in a format that is not in the arrangement between the countries, until another notification is received from the relevant authorities in the State of Israel.

Dodd-Frank Wall Street Reform and Consumer Protection Act (DFA)

The Dodd-Frank Wall Street Reform and Consumer Protection Act (DFA) is an American Federal Law which came into force on 21 July 2011 and implements a comprehensive reform of financial regulation, with various implications for Bank Leumi, the main points of which relate to over-the-counter (OTC) swap derivative transactions.

Title VII of the DFA authorizes the United States Securities Exchange Commission (SEC)– in relation to security-based swap derivative transactions in derivatives - and the Commodity Futures Trading Commission (CFTC) – in relation to the rest of the swap derivative types of transactions - to carry out various transactions, most important of which are:

The implementation of cross-border regulation of traders in swap derivative transactions, the aim of which is, *inter alia*, the duty of registering as swap dealers, or as a major swap participant in the National Futures Association (NFA) of anyone whose total transactions exceeds a pre-defined threshold with effect from 12 October 2012, the holding of a minimum capital and management of collateral (margin), the placing of standards for business behavior, the application of the duties of documenting transactions, furnishing the related reports, etc.

According to the Bank's examinations, as of today, the Bank is under the threshold requiring a duty of registration mentioned above.

The reform is intended to increase transparency in the derivatives market, through the application of the duty of trade in swap transactions in derivatives under trading platforms, the provision of publicity for these transactions through the duty of reporting to central databases which will be accessible to all market players, and the strengthening of competition as a consequence thereof.

The reduction of the risk reflected by swap derivative transactions through the application of the duty of clearing them through central clearinghouses, which will function as intermediaries and as "absorbing" the risk of insolvency of whichever of the parties to the transaction, similar to the use made of them in the past in the field of futures transactions.

In the context of this duty, the Bank is now concluding an arrangement with a foreign bank which is a member of the central clearinghouse for clearing swap transactions and is examining further engagements with another clearinghouse member.

European Market Infrastructure Regulation (EMIR)

At the same time as the DFA, the European Union published the EMIR, which contains principles similar, but not identical, to DFA, and is intended to contend with the same systemic risks as those reflected by over-the-counter traded derivative transactions. The EMIR applies, *inter alia*, to European financial entities, similar duties to those applied under the DFA (clearing, reporting, and management of collateral).

The implementation regulations of EMIR have not yet been fully completed.

In order to prepare for the implementation of the DFA and EMIR in Leumi Group, the Bank has set up a steering committee to study and monitor the development of the relevant legislation under them and the expected timetable for the inception of their various regulations. In order to ensure early preparedness for is implementation, the steering committee is managed by the Capital Markets Division, with regular consultation with accountants and with consultation on specific issues with the Legal Counsel Division and foreign law firms.

Most of the duties by virtue of DFA and EMIR apply to the Bank indirectly because of its engagement with American and/or European financial institutions, which are obliged to comply with them. In addition, from time to time, the Bank is requested by American and/or European counterparties to approve its attachment to various protocols of the International Swaps and Derivatives Association (ISDA), with the intention of guaranteeing the counterparties fulfilling the duties under the DFA and the EMIR.

The subject of reconciliation came into force in September 2013. Bank Leumi signed the ISDA Portfolio Reconciliation for adapting a portfolio and applies this on a daily basis.

The subject of reporting will come into force in February 2014. Bank Leumi signed the ISDA Reporting Protocol in 2013, and enables European banks to report on transactions they carry out vis-à-vis Bank Leumi.

The subject of central clearing in certain transactions is expected to come into force at the end of 2014.

Taxation

Company tax

On 30 July 2013, the Knesset plenum approved the Economic Program for 2013-2014 (Budget Law) which includes, *inter alia*, an increase in company tax from 25% to 26.5%, with effect from 1 January 2014.

The change in the company tax rate in the Budget Law as aforesaid, and the change in the rate of profit tax as detailed below, will increase the statutory tax rate applicable to all financial institutions from 36.21% in 2013 to 37.71% in 2014 and thereafter.

The change in the company tax rate resulted to an increase in net deferred tax balances receivable amounting to NIS 107 million.

Value added tax and national insurance

On 28 May 2013, the Minister of Finance signed an order raising the rate of value added tax in respect of a transaction and the import of goods from 17% to 18%, with effect from 2 June 2013.

On 2 June 2013, the Value Added Tax Order (Rate of Tax on Non-Profit Associations and Financial Institutions) (Amendment), 2013 was published, updating the rate of profit tax and salary tax imposed on financial institutions from 17% to 18%. As a result of the said change, the statutory rate of tax applicable to financial institutions increased in 2013 from 35.9% to 36.21%. Furthermore, the rate of salary tax applicable to financial institutions increased from 17% to 18% with respect to the salary payable for work in June 2013 and onwards.

The change in the rate of profit tax has led to an increase in net balances of deferred tax receivables amounting to NIS 30 million in the second quarter of 2013. The effect of the increase in salary tax on the balance of liabilities to employees as at 30 June 2013 is NIS 53 million before tax and NIS 34 million after tax.

The change in salary tax resulted in an increase of NIS 56 million in current salary expenses and operating expenses in 2013, compared with 2012.

On 13 August 2012, the Deficit Reduction and Change in Tax Burden Law (Legislative Amendments), 2012 (hereinafter "the Law"), was published. Pursuant to the Law, with effect from January 2013, the rate of national insurance contributions collected from employers in respect of the portion of the salary exceeding 60% of the average salary in the economy increased from 5.9% to 6.5%. In addition, it was provided that this rate would increase to 7% and 7.5% in January 2014 and January 2015, respectively. However, on 27 January 2014, the Reliefs in the Capital Market and Encouragement of Activity Therein (Legislative Amendments), 2014, was published according to which the rate of insurance fees collected from employers in respect of the part of salary exceeding 60% of the average salary in the market, will be updated in January 2014, January 2015 and January 2016 to 6.75%, 7.25% and 7.5%, respectively.

Consortium Arrangements for the Granting of Credit

On 26 February 2013, the effective period was extended for a letter of the Antitrust Commissioner to managers of banks and insurance companies setting out the conditions that if fulfilled, the Antitrust Authority does not intend to enforce the provisions of the Antitrust Law, 1988 ("the Law"), regarding association between the banks and insurance companies and between them and themselves ("banks and institutional entities") in a credit consortium.

A summary of the conditions for forming a consortium for the provision of credit is as follows:

1. The formation of the credit consortium must be with the written consent of the customer on a separate form;

2. The customer is given the option of negotiating over the terms of the provision of credit with any one of the member parties in the consortium, including through another person on its behalf;

3. The formation of a consortium in which both Bank Hapoalim B.M. and Bank Leumi Le'Israel B.M. are members will be permitted only if the aggregate amount of the credit that the two banks are required to grant exceeds NIS 300 million (except for the case of a consortium arrangement whose purpose is the repayment of a debt deriving from credit provided by the aforesaid two banks before 18 August 2002 to the same person).

4. Any information that is not required for the purpose of forming the specific consortium in respect of which the contacts are maintained may not be transferred between the parties. Any transfer of information as aforesaid will be made in a way that minimizes any chance of impairment to competition between the parties.

5. The parties will prepare documentation that must include all of the data as outlined in the Commissioner's notice, both with regard to contacts made and/or information transferred between the parties on matters relating to the formation of a credit consortium, and with regard to a credit consortium that actually exists and with regard to contacts that did exist but have not actually resulted in a credit consortium. The documentation must be retained with each bank and/or institutional entity and transferred to the Authority within 30 days of the end of each calendar year, and on demand within 14 days of the demand.

The said validity of the Commissioner's notice was extended for an additional year until 30 June 2014, unless another notice is issued before the end of the effective period.

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

The Director's Report includes, as mentioned above, in addition to data relating to the past, information that relates to the future, which is defined in the Securities Law, 1969, ("the Law") 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 with 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 programs", "the Bank's forecast", "expected", "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 a past fact.

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 currency markets and the capital markets, to legislation, to directives of regulatory bodies, to the behavior of competitors, to technological developments and to personnel matters.

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 in this Report.

The above does not detract from the reporting duties of the Bank under the law.

Accounting Policy on Critical Subjects

General

The preparation of consolidated financial statements, in accordance with generally accepted accounting principles and the directives of the Supervisor of Banks, requires Management to make estimates and assessments that affect the reported amounts of assets and liabilities and the amounts of income and expenses.

The estimates and assessments are generally based on economic forecasts, assessments regarding the various markets and past experience, while exercising discretion, on which management believes to be reasonable at the time of signing of the financial statements.

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

The principal accounting policies applied in the Leumi Group are set out in detail in Note 1 to the Financial Statements.

Set out below is a brief description of the major critical accounting subjects which involve Management's estimates and assessments and which have been discussed by the Board of Directors, Management and the joint auditors:

Allowances for credit losses and classification of problem debts

Directives for the measurement and disclosure of impaired debts, credit risk and allowance for credit losses

Collective allowance

The collective allowance for credit losses is applied to large groups of relatively small and homogenous debts, and in respect of debts that have been reviewed individually and found to be unimpaired. The measurement of the credit losses is based on the transitional provisions as set forth below. The collective in respect of off-balance sheet credit instruments is based on the rates of allowance determined for balance sheet credit, taking into account the rate of recovery for the expected credit of off-balance sheet credit risk.

The rate of realization for the credit is calculated by the Bank based on credit conversion coefficients, as provided in the Proper Conduct of Banking Business no. 203, Measurement and Capital Adequacy – Credit Risk – the Standardized Approach, with certain adjustments in cases where the Bank has past experience indicating the recovery rates of the credit.

For 2011-2013, a temporary provision was given ("transitional period") for calculating the collective allowance. According to the temporary provision, the allowance rates will be determined in the transitional period on the basis of the range of the historical rates of provision for doubtful debts in the years 2008-2010 and on the percentage of net accounting write-offs actually recorded since 1 January 2011, in a breakdown according to market sectors. In addition to the calculation of the range of historical rate of loss in various economy sectors, as aforesaid, for the purposes of determining the fair rate of allowance, the Bank takes into account additional information, including sectoral conditions, macro-economic data, a general assessment of the quality of the credit and various additional effects (such as credit concentrations).

With regard to housing loans, a minimum allowance for doubtful debts is calculated according to the formula set by the Supervisor of Banks, taking into account the extent of arrears, such that the rates of allowance increase as the arrears deepen. The application of the calculation of the allowance according to the extent of arrears formula refers to all housing loans, except for loans which are not repaid in periodic installments and loans which finance activity of a business nature. In addition, a collective allowance is made on the balance of the housing loans in which there are no arrears, based on past statistics (subject to a minimum rate determined by the Supervisor of Banks).

The Bank examines the accuracy of the collateral allowance based, *inter alia*, on the assessment or risks inherent in the credit portfolio and an examination of the trends and developments in the main segments.

With regard to the draft circular updating the Public Reporting Directives, "Collective Allowance for Credit Losses", see below in the financial statements, note 1X(4).

In addition, the Bank calculates a supplementary and general provision according to the policy for the doubtful debt provision before implementing the provisions regarding impaired debts, credit and credit loss allowance. This calculation acts as an indication with regard to the collective allowance, so that it is possible to ensure that the collective allowance is higher than the supplementary and general provision, at least compared to that required according to Bank of Israel directives.

Individual allowance

Within the context of the Bank's credit policy, principles have been determined for the granting of credit and the administration and supervision of the Bank's credit portfolio, with the aim of improving its quality and reducing the risk inherent in its management. The Bank examines the credit portfolio on an ongoing basis and in accordance with procedures, for the purpose of identifying, as early as possible, those borrowers whose risk level and exposure have risen and who require special management attention and close monitoring, in light of the characteristics of the risk or as a result of the economic/market conditions that are likely to impact the borrowers' condition, so as to improve their position. An assessment of the extent of the problem is made while exercising business judgment by the business entities dealing with the borrower, by the credit risk management units in the Risk Management Division, as well as an objective evaluation of the difficulties that have been identified, in order to determine their risk level.

In the Banking Division, customers with an obligo of more than NIS 1 million are individually identified and reviewed, and the remainder is dealt with as a group of homogenous and relatively small debts, making a collective allowance.

As part of the measures used by the Bank to manage credit risk, there is a methodology for identifying and classifying problem debts, which the Bank implements in all its lines of business. The methodology includes a structured quarterly work process in the context of which a thorough review of the credit portfolio is carried out on the basis of a number of criteria that give advance warning of a debt becoming problematic, as part of a process of dealing with customers defined as "sensitive customers". A quarterly credit review process is carried out in the Corporate and Commercial Division and in the International Credit and Real Estate Division, which deal with the larger customers of the Bank and medium-sized business corporations, a quarterly credit review process is carried out, in which borrowers whose risk rating is higher than that requiring inclusion in the customer population defined as sensitive. *Inter alia,* the methodology requires systematic examination of the appropriateness of the allowance for credit losses in respect of the debts regarding the collection of which the Bank has doubts, on the basis of criteria established for the manner in which the allowances for credit losses are to be calculated, determined in accordance with the directive. An examination of the accuracy of the allowance is made every quarter, for all lines of business, for customers classified as "impaired". The calculation is made in accordance with the characteristics of the debt, the assessment of future cash flows based on the customer's financial position and his ability to continue to operate, the business environment in which the customer operates and the degree to which the customer meets its obligations, together with past experience and a realistic examination of the collateral and the ability to realize them, and all this, in the capitalized value of the discounted receipts and the fair value of the realization of the collateral, in the judgment of the authorized factors. The credit risk management units and the corporate credit branch in the Banking Division approve the examination of the appropriateness of the allowance. In addition, an examination is made of the ability to service the debt of customers classified by other debt indicators (debt under special mention and substandard debt).

The process described above for classifying debts and estimating potential losses in the credit portfolio involves subjective assessments in all matters connected to the classification of a loan as problematic and to the factors on which the calculations of allowances are based. The assumptions and estimates may have a material effect on the amount of provisions for credit losses.

Each quarter, the Bank's Allowances Committee, headed by the Chief Executive Officer, discusses the allowances required for the quarter and the recommendations for the classification of problem loans. Proposals for the quarterly allowances in excess of NIS 2 million required for customers are presented for discussion. In addition, the Audit Committee of the Board of Directors discusses the allowances for credit losses so as to approve their amount. Data on the debts and collateral of the major customers in respect of whom an allowance is required, as well as the amounts of allowance proposed by Management, are made available to the Directors as background material.

The allowances of consolidated Israeli subsidiaries are determined by the authorized factors and made in accordance with the generally accepted principles in the Bank and in accordance with the Bank of Israel directive, with regard to banking corporations.

The allowances of overseas consolidated subsidiaries are determined by their authorized bodies, in accordance with accepted practice in the countries in which they operate and the directives of the local regulatory authorities.

Derivative instruments

In accordance with the directives regarding financial reporting of the Supervisor of Banks, the Bank applies Financial Accounting Standards nos. 133, 138, 149 and 157, all as amended, with regard to the treatment and presentation of derivatives.

Fair value is defined as an amount/price which would be received from the sale of an asset or would be paid for the transfer of a liability in a transaction between a willing buyer and a willing seller at the measurement date. Among other things, the standard requires for the purpose of the assessment of fair value to make maximum use of observable data and minimum use of unobservable data. Observable data represent information which is available in the market received from independent sources, while unobservable data reflect the banking corporation's assumptions.

FAS 157 outlines a hierarchy of measurement techniques which are based on the determination of whether the data employed for determining the fair value are observable or unobservable. These kinds of data create a scale of fair value as set forth below:

- Level 1 data: quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2 data: quoted prices for similar assets or liabilities in active markets; quoted prices for identical assets or identical liabilities in inactive markets; prices derived from valuation models where all of the significant data is observable in a market or supported by observable market data.
- Level 3 data: Unobservable data for the asset or the liability deriving from valuation models, where one or more of the significant figures are unobservable.

This hierarchy requires the use of observable market data, where this information exists. When this is possible, the Bank weighs relevant observable market information as part of its assessment. The scope and frequency of the transactions, the size of the gap between "bid" and "ask" prices and the size of the adjustment required when comparing similar transactions are all factors that are taken into account when establishing the liquidity level of markets and the relevant scope of observable prices in those markets.

The level in the fair value scale to which the fair value measurement of the financial instrument belongs will determined on the basis of the lowest level of the data which is significant to the measurement of the fair value in its entirety.

The standard requires that the banking corporation reflect the credit risk and the risk of non-performance risk in measuring the fair value of the debt, including derivative instruments, which were issued by it and measured at fair value. Non-performance risk includes the credit risk of the banking corporation.

In accordance with the transitional provisions for 2012, which were also extended to 2013, specific directives regarding the methodology and data to used in calculating the fair value of derivative instruments were determined. A banking corporation is not required to employ complex models including various scenarios of potential exposure in order to measure the credit risk component included in the fair value of derivative instruments. According to the abovementioned transitional provisions, and pursuant to the directives of the Supervisor of Banks, the Bank performs the calculation of the adjustment as aforesaid on a customer level, using a credit quality index based on internal models or on market data.

In a few cases where the Bank does not have a mathematical model for revaluing a derivative, the fair value is determined on the basis of price quotations received from traders in such derivatives. Although these quotations are received from reliable brokers with whom the Bank has chosen to work, it is not certain that the price quoted reflects the price obtainable in an actual transaction in any amount, and especially a transaction in a large amount.

For further details with regard to the determination of fair value, see Note 1H.

Securities

Securities, other than debentures held to maturity, are presented in the balance sheet at fair value. Shares in respect of which the fair value is not available are presented at cost.

The fair value of Israeli securities is based primarily on prices quoted on the Tel Aviv Stock Exchange, and of overseas securities, on prices received from external sources. With regard to foreign securities, most of the portfolio is calculated on a daily basis by a reputable international body which is engaged in the business of calculating the fair value of financial assets for their disclosure in the financial statements. This organization is not dependent on the issuing houses or the marketing bodies. The calculation is based mainly on the transaction prices in active markets, and the revaluation of similar transactions. The calculation reflects the price that a willing buyer in the market would pay for securities, based on current information available in the market. Due to the fact that only a small part of the securities is traded worldwide on a daily basis, the organization makes use of two valuation methods:

a. Valuation at the level of asset group: Most of the securities are valued using rates of return (capitalization) relating to the group of assets with similar characteristics and by country, sector, asset type, rating etc.). This mainly includes, a weighting of the existing information in the market, usually in relation to the relevant index.

b. Valuation and quotations for specific securities: The rest of the securities are valued individually (valuation of the issuer and the individual security), on the basis of direct price quotations of the security or for a specific issuer. A small portion of the assets in this group is valued only on the basis of price quotations from very active markets (mainly government debentures, whose market-0makers are active).

In non-tradable securities of companies in Israel, fair value is based on data received from the "Mirvach Hogen" company. Sometimes, for reasons of prudence, when there are indicators, the Bank adjusts the model and/or market price in order to establish a more accurate value.

For further details, see the chapter, "Structure and Development of Assets and Liabilities, Securities", see below.
For further details with regard to the determination of the fair value, see Note 1H.

The Bank examines the necessity for recording a provision for impairment of securities that is not of a temporary nature. The examination is carried out when there are signs which indicate the possibility that the value of the securities has been impaired. The criteria for determination as to whether an impairment is not of a permanent nature are based on considerations and tests as follows:

- An intention and an ability to strengthen the security until the predicted recovery of the full amount of the cost.
- The assets and collateral backing the security.
- The ratio of the impairment to the total cost of the security.
- The length of time for which the fair value has been lower than cost.
- An assessment of repayment ability.
- An adverse change in the situation of the issuer or in the situation of the entire market.

The Bank's policy is to recognize a decline in value as being non-temporary in nature if one or more of the following conditions are met:

1. A security that was sold before the date of the publication of the Report to the public.

2. A security that the Bank intends to sell, as of a time close to the date of the publication of the Report to the public, within a short time frame.

3. A debenture whose rating was significantly downgraded between the rating at the date of its purchase by the banking corporation and the rating at the date of the publication of the Report. Reduction of the rating below BBB- only is considered a significant downgrading for purposes of this section.

4. A debenture which, after its purchase, was classified as problematic by the Bank.

5. A debenture for which there was a credit failure that was not corrected within a short period of time.

6. A security, the fair value of which has been lower than the value at which it was purchased, for a period of at least nine months prior to the end of the reported period, and is lower, by 35% or more, than the cost at the end of the reported period, as well as at a date prior to the publication of the report (regarding debentures – the adjusted cost).

Exceptions are allowed in such cases, if the Bank has objective and solid evidence and a cautious analysis of all relevant factors, which establishes, with a high degree of certainty that the decline in value is of a temporary nature. The objective evidence and relevant factors include parameters such as: a rise in value after the date of the financial statement, a high credit rating (group A or above), analysis of stability in stress scenarios by an external professional body or by the Bank, its backing including direct government investment in the equity for the purpose of ensuring the strength of the issuing bank.

These principles conform to the guideline issued by the Supervisor of Banks. The definitions of "significant downgrading" and "significant impairment" have been determined by the Bank.

Obligations regarding Employee Rights

The amounts of the obligations for pension and long-service grants are currently calculated according to actuarial models, using a capitalization rate of 4% (index-linked) and determined by the Supervisor of Banks. In addition, the actuarial computations take into account the forecast real increase in pay on the basis of past experience, which varies according to the age of the employee. The rates of increase vary between 0.6% and 7.3%.

Quantitative sensitivity analysis of the effect of main assumptions in the calculation of the actuarial liability is as follows:

A decrease of 1% in the rate of capitalization of the abovementioned liabilities will result in an increase of NIS 2 billion in total liabilities. A decrease of 1.0% in the increase of salary will result in a reduction of NIS 589 million in total liabilities. An increase of 5.0% in the life expectancy will result in an increase of NIS 120 million in total liabilities. All amounts are before the effect of tax.

The actuarial models include assumptions regarding life expectancy tables, disability rates, leaving rates, the rate of leaving with preferred conditions, the rate of utilization of pension rights, the rate of withdrawal of severance pay and provident fund monies, etc. Although the parameters have been determined with appropriate care and professional expertise, a change in any or some of the actuarial parameters and/or the capitalization rate and/or the rate of increase in pay will cause a change in the level of the Bank's obligations.

The actuarial changes resulting either from changes of actuarial parameters, or from the change in the yield of the reserves that are used to cover liabilities, are recorded in the profit and loss statement. In contrast, at the U.S. and British subsidiaries, these changes are charged to capital fund, in accordance with the accounting rules in those countries. For the purpose of the consolidated financial statements, the recording in the capital fund is cancelled and the amount is recorded in the profit and loss statement.

The actuary's valuation of the employees' rights may be found on the Israel Securities Authority's website, the address being: www.magna.isa.gov.il.

On 30 January 2014, the Banking Supervision Department published a draft regarding the adoption of United States accounting principles on the subject of employee rights. The draft updated the recognition, measurement and disclosure requirements on the subject of employee benefits in the Public Reporting Directives in accordance with accounting principles generally accepted in banks in the United States. This draft includes certain updates in the Public Reporting Directives, but does not include all of the updates required for the directives as a result of the adoption of these principles. These subjects, including additional interpretations, if necessary, will be dealt with separately.

The draft provides that the amendments to the Public Reporting Directives will apply from 1 January 2015 when, on initial implementation, the Bank will retroactively amend the comparative figures for periods commencing 1 January 2013 and thereafter, in order to comply with the requirements of the principles, inter alia, in accordance with the provisions of the draft.

- The cost of capital for computing the liability in respect of employee rights will be based on the market yield of government debentures in Israel. As a result, the temporary provision in the existing directives which determine the cost of capital for computing reserves to cover employee rights, will be canceled.
- A banking corporation should apply the accounting principles generally accepted in the United States on the subject of share-based payments as stated in ASC 718 – Compensation – Stock Compensation.

Pursuant to the draft published by the Department, a bank is required to provide at least disclosure in the 2013 financial statements of an estimate of the quantitative effect on shareholders' equity of the computation of the liabilities due to employee rights using costs of capital based on market yield at the reporting date of government debentures in Israel. According to the Bank, while the standard is being implemented on 31 December 2013 in accordance with the present interest environment, the expected effect on the shareholders' equity of the Bank at 31 December 2013 in respect of the effect of the change in the cost of capital only is a reduction of NIS 2.3 billion (NIS 3.7 billion before tax). It is understood that this liability will be updated in accordance with changes in the relevant market interest in future years.

It should be clarified that the adoption of U.S. accounting principles on the subject of employee rights is like to have other effects on the Bank's capital, which we are studying. One of those possible effects is the method of accruing liabilities. From estimates and preliminary interpretations, the effect of the change in the accrual of liabilities is liable to result in a further reduction in shareholders' equity of NIS 0.25 billion after the effect of tax (NIS 0.4 billion before tax). The Bank is examining additional interpretations for the spread of liabilities and/or the additional effects that are also likely to materially alter these estimates.

Despite the material adverse effect on shareholders' equity, for the purpose of computing the capital requirements pursuant to the Basel III directives, in accordance with the transitional provisions stipulated in Proper Conduct of Banking Business Management Directive no. 299, the accrued balance of the profit or loss in respect of remeasurements of the net liabilities or net assets in respect of a employee-defined benefit will not be brought into account immediately, but will be subject to transitional provisions, over a number of years.

Obligations in respect of legal claims

Among the Bank’s other obligations, there are provisions for various legal claims against the Bank, including applications for class actions. The provisions were determined in a conservative manner in accordance with Management’s assessments, based on legal opinions.

A quarterly discussion is held in the Bank's Allowance Committee, headed by the President and CEO, and in the Board of Directors in respect of provisions for claims above a certain amount that have been filed against the Bank.

To assess the risks in legal proceedings filed against the Bank, the Bank’s Management relies on the opinions of the outside counsel representing the Bank in these claims.

These opinions were given by the outside counsel in accordance with their most considered opinion on the basis of the facts presented to them by the Bank and on the basis of the known legal position (laws and case law) as at the date of the assessment, and which are often open to possible conflicting interpretations and claims.

The assessment of risks inherent in requests for the approval of class actions is complex, since this is a field, the legal doctrine relating to which, even on important matters of principle, is still being formed and not yet entirely settled. There are also claims in respect of which, due to the stage of the proceedings, counsel is unable to estimate their inherent risk, even under the above-mentioned limitations.

In light of the above, it is possible that the actual results of claims may differ from the provisions made.

Buildings and Equipment

The Bank's buildings and equipment are presented in the financial statements at cost, less accumulated depreciation and a provision for a decline in value.

Buildings offered for sale are presented at the lower of their cost or realization value. The realization value is determined by assessors. Changes in the valuation of the asset may affect the amount of the provision for impairment of assets offered for sale.

Depreciation is calculated on the basis of the cost, in accordance with the estimated use period, according to the straight line method. Direct costs relating to the development of computer programs for own use (as defined in International Accounting Standard No. 38 – "Intangible Assets") are capitalized as investments in equipment after the conclusion of the initial planning stage of the project and are depreciated from the date of their operation according to an assessment of the period of their use.

From time to time the management of the Bank examines the need for provisions for a decrease in value of the assets owned by the Bank. The test for a decrease in value of the assets is made by comparing the book value of the asset with its recoverable amount. Recoverable value is the higher of the realization price of the asset and its usage value (which is the present value of an estimate of the forecasted future cash flows from the use of the asset).

Taxes on income

The Group has implemented the International Standard IAS 12, as provided in the Public Reporting Directive "Taxes on Income" with effect from 1 January 2012.

Current taxes and deferred taxes are charged to the statement of profit and loss, or carried directly to capital, if they derive from items that are recorded directly in capital.

The current tax is the amount of tax expected to be paid (or received) on taxable income for the tax year, calculated at the tax rates applicable according to the laws enacted up to the balance sheet date.

Deferred taxes

The recognition of deferred taxes receivable/payable is with regard to temporary differences between the book value of assets and liabilities for financial reporting purposes and their value for tax purposes. Deferred taxes are measured at the tax rates expected to be applicable to the temporary differences at the date they are realized, based on the laws enacted until the balance sheet date.

A deferred tax asset in respect of carryforward losses, tax benefits and temporary differences allowable is recognized in the books when it is more likely than not that, in the future, there will be taxable income against which it will be possible to utilize them.

The Group does not record deferred taxes in respect of profits from investments in investee companies which the Bank intends to hold and not realize, and also in respect of dividends that are not expected to be distributed by investee companies.

Disclosure regarding Procedure for Approval of the Financial Statements and Disclosure Policy

Procedure for 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. Most of the members currently serving on the Board of Directors possess accounting and financial expertise (14 out of 15 directors).

Discussions on the financial statements (recommendation to the Board of Directors with regard to their approval) are conducted in the Audit Committee of the Board of Directors, pursuant to the provisions of Regulation 301 of the Supervisor of Banks.

Before the financial statements are submitted to the Audit Committee for discussion, the Bank's financial statements are discussed by the Disclosure Committee. The Disclosure Committee is a management committee comprising members of the Bank's Management, the Chief Internal Auditor and additional senior managers of the Bank. The Disclosure Committee checks, *inter alia*, that the information in the financial statements is accurate, complete and presented fairly. (The Disclosure Committee was set up as part of the implementation of the Bank Supervision Department directive, which is based on Section 302 of the Sarbanes-Oxley (SOX) Law. See the chapter, "Controls and Procedures with regard to Disclosure in the Financial Statements", below.

Prior to the discussion of the financial statements by the full Board of Directors, discussions are held by the Audit Committee, with the participation of the President and Chief Executive Officer, the Head of the Finance and Economics Division, the Chief Accounting Officer, the Chief Internal Auditor and others.

The background material sent to the members of the Audit Committee for discussion includes the minutes of discussions in the Disclosure Committee and its decisions, the draft Board of Directors' Report, the draft of the Management Review, the draft of the Financial Statements, information regarding the Bank's exposure to legal claims and a description of the new legal claims, and background material for discussion on the appropriateness of the classification of problem customers and the provisions. In addition, a draft corporate governance questionnaire is included in the background material in anticipation of discussions on the periodic reports. The members of the committee also receive details of new disclosure requirements (if any) applicable to the Bank.

As part of the deliberations of the financial statements, the Audit Committee discusses the appropriateness of the provisions and the classifications of the Bank's problem debts, after the Chief Executive Officer has presented to the committee the extent of the provisions and the classification for problem debts and the changes and the trends in this area, and after the senior managers have presented the extent of the provisions and classifications for which they are responsible and have detailed the main factors of change in these areas. The subject of the legal claims and of the Bank's exposure in this regard is presented by the Bank's Chief Legal Advisor. The Chief Accountant presents to the Committee the main and material matters in the Directors' Report and Financial Statements, the changes in critical accounting policies, if any, and the main matters discussed by the Disclosure Committee, and the Committee also discusses these matters. If necessary, the subject of impairment of securities is presented by the senior manager from the Capital Market Division. If necessary, the subject of decline in value of the securities is presented by a senior manager from the Capital Market Division.

The Audit Committee submits its recommendations regarding the financial statements to the Board of Directors. The committee's recommendations relate, *inter alia*, (in accordance with the provisions of the Companies Regulations (Directives and Conditions Regarding the Process for Approving the Financial Statements), 2010) ("**the Companies Regulations**") to assessments and estimates made in connection with the statements; internal controls related to financial reporting, completeness and fairness of disclosure in the statements; the accounting policy adopted and the accounting treatment applied on the Bank's material interests; valuations, including assumptions and estimates on which they are based, which support the data in the financial statements.

Following the discussions on the financial statements in the Audit Committee, there is discussion on the final draft of the financial statements in the full Board of Directors, attended by the President and Chief Executive Officer, the Head of the Finance and Economics Division, the Chief Accounting Officer, the Chief Internal Auditor, and when the discussion concerns the approval of the annual financial statements, all the other members of the forum of the Bank's Management. As background material for the discussion, the Directors receive the draft financial statements together with extensive accompanying background material, including in-depth comprehensive analyses of the Bank's activities in its various areas of business.

In the context of this discussion, the Bank's President and Chief Executive Officer reviews the results of Leumi Group's operations and the Chief Accountant presents and analyzes the results of the Group's operations in Israel and abroad, including a description of risk exposure and compliance with the limits established with regard to such risks. Thereafter, the full Board of Directors discusses and accordingly approves the financial statements.

All the discussions of the Board of Directors, the Audit Committee and the Disclosure Committee regarding the financial statements are attended by 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 their presentation to the joint auditors to the Audit Committee of the Board of Directors in their discussions of the financial statements, any material weaknesses that may have arisen during the audit processes that they carried out, and after the Board is presented with the representations of the President and Chief Executive Officer, the Head of the Finance and Economics Division and the Chief Accountant regarding evaluation of the Bank's disclosure controls and procedures for the financial statements.

The composition of the Audit Committee is as stipulated by the Companies Law Regulations. The committee includes seven directors, including, pursuant to the Companies Law, three external directors, including a chairman of the committee. A further two committee members are external directors as stipulated by the Banking Supervision Department, and all the aforesaid external directors (pursuant to both Companies Law and the Banking Supervision Department Regulations) are independent directors. In addition, all committee members have financial and accounting expertise. The Chairman of the Board of Directors participates as an observer in meeting of the Audit Committee on matters related to the financial statements.

Disclosure Policy

Pursuant to Bank of Israel directives, the reporting requirements in Pillar 3 of the Basel II directives oblige the Bank to determine a formal disclosure policy. The policy is to refer to the banking corporation's approach to determining what disclosure is made, including the internal controls on the process.

Leumi has determined its disclosure policy, which has been approved by the Board of Directors.

The disclosure policy is based on the Directives for Reporting to the Public of the Supervisor of Banks and the provisional directives of the Israel Securities Authority, which have been adopted by the Supervisor of Banks.

In accordance with the said disclosure policy, Leumi aims to provide all material information necessary to understand its statements, which will be reported clearly and in detail.

Information given in the Directors' Report is prepared in accordance with directives for Reporting to the Public, particularly with regard to "Temporary Order concerning the Description of the Banking Corporation's Business and Forward-Looking Information in the Directors' Report". In accordance with the directive, the directors' report is to include information in the Bank's business, the operating segments in which it operates, the general environment in which it operates and its effect on the Bank, the control structure of the Bank and its organizational structure, legal proceedings, material agreements, and detailed information on other matters.

With regard to information which can be quantified monetarily, quantitative data is given, and with regard to other information, qualitative data is given.

The general principle according to which information is given in the report is the principle of materiality. The Bank's business and its activities are examined according to their scope and nature, and at the end of the examination, disclosure is made regarding matters of material monetary size in relation to the annual profit of the Bank with regard to profit and loss items, its assets or its capital with regard to balance sheet items. In addition, disclosure is made of matters of public interest or of special sensitivity, such as matters connected with the structure of the Bank, its management, legislation affecting the bank and so on.

For the purposes of complying with this policy, every material subject is brought for discussion to the Disclosure Committee, (see above chapter, "Procedure for Approval of the Financial Statements"), which decides, in all dubious cases, whether to make the necessary disclosure. In addition, the Disclosure Committee discusses the findings of the review of the examinations of the financial reporting control.

Minutes of the Disclosure Committee are sent for perusal by the members of the Audit Committee of the Board of Directors.

See also the chapter, "Controls and Procedures regarding Disclosure in the Financial Statements", below.

D. Description of the Group's Businesses according to Segments and Areas of Activity

Development of Income, Expenses and Tax Provision[1]

The net profit attributable to the shareholders of the banking corporation (hereinafter "net profit") of Leumi Group in 2013 amounted to NIS 1,947 million, compared with NIS 931 million in 2012 – an increase of 109.1%.

The increase in net profit in 2013, compared with 2012 is explained as follows:

	For the year ended 31 December *			
	2013	2012	Change	
	NIS millions		NIS millions	%
Net interest income	**7,357**	7,408	(51)	(0.7)
Expenses in respect of credit losses	**(268)**	(1,236)	968	78.3
Noninterest income	**5,517**	4,774	743	15.6
Operating and other expenses	**(8,933)**	(9,100)	167	1.8
Profit before taxes	**3,673**	1,846	1,827	99.0
Provision for tax	**(1,391)**	(811)	(580)	(71.5)
Profit after taxes	**2,282**	1,035	1,247	120.5
The Bank's share in losses of companies included on equity basis	**(293)**	(67)	(226)	-
Net profit attributable to holders of non-controlling interests	**(42)**	(37)	(5)	(13.5)
Net profit attributable to shareholders of the banking corporation	**1,947**	931	1,016	109.1

* The symbols are according to their effect on net profit.

(1) The financial statements are prepared in reported values. The known consumer price index rose by 1.9% in 2013. The shekel appreciated in nominal terms by 7.0% against the U.S. dollar, and against the euro by 2.8%. The representative rate of exchange of the U.S. dollar on 31 December 2013 was NIS 3.471.

For further details see note 1(E) to the financial statements.

The profit of the Leumi Group in the fourth quarter of 2013 amounted to NIS 348 million, compared with a loss of NIS 259 million in the corresponding period last year.

	For the three months ended 31 December *			
	2013	2012	Change	Change
	NIS millions		NIS millions	%
Net interest income	**1,810**	1,784	26	1.5
Expenses in respect of credit losses	**(155)**	(386)	231	59.8
Noninterest income	**1,420**	1,394	26	1.9
Operating and other expenses	**(2,254)**	(2,611)	357	13.7
Profit before taxes	**821**	181	640	+
Provision for tax	**(299)**	(233)	(66)	(28.3)
Profit (loss) after taxes	**522**	(52)	574	+
The Bank's share in the profits (losses) of companies included on equity basis	**(165)**	(199)	34	17.1
Net profit attributable to holders of non-controlling interests	**(9)**	(8)	(1)	(12.5)
Net profit (loss) attributable to shareholders of the banking corporation	**348**	(259)	607	+

* The symbols are according to their effect on net profit.

For details on changes, see below.

'

The following is the condensed statement of profit and loss for the eight last quarters:

	2013				2012			
	4th quarter	3rd quarter	2nd quarter	1st quarter	4th quarter	3rd quarter	2nd quarter	1st quarter
	NIS millions							
Net interest income	**1,810**	1,946	1,839	1,762	1,784	1,872	1,924	1,828
Income (expenses) in respect of credit losses	**(155)**	44	(84)	(73)	(386)	(292)	(333)	(225)
Non-interest income	**1,420**	1,382	1,246	1,469	1,394	1,208	995	1,177
Operating and other expenses	**(2,254)**	(2,443)	(2,179)	(2,057)	(2,611)	(2,294)	(2,200)	(1,995)
Profit before taxes	**821**	929	822	1,101	181	494	386	785
Provision for taxes	**(299)**	(345)	(284)	(463)	(233)	(113)	(159)	(306)
Profit after taxes	**522**	584	538	638	(52)	381	227	479
Group’s share in operating profits (losses) of companies included on equity basis	**(165)**	(17)	(54)	(57)	(199)	108	63	(39)
Net profit (loss) attributable to holders of non-controlling interests	**(9)**	(12)	(10)	(11)	(8)	(10)	(10)	(9)
Net profit (loss) attributable to shareholders of the banking corporation	**348**	555	474	570	(259)	479	280	431

Net interest income of Leumi Group in 2013 amounted to NIS 7,357 million, compared with NIS 7,408 million in 2012, a decrease of NIS 51 million, or 0.7%. The decrease is primarily attributable to the low interest rates on the various markets, partially offset by the increase in the balances of the income-yielding monetary assets.

In the fourth quarter of 2013, net interest income amounted to NIS 1,810 million compared to NIS 1,784 million in the corresponding period in 2012, an increase of 1.5%.

The ratio of net interest income to the average balance of income-bearing assets is 2.24% (in annual terms) compared to 2.27% in the corresponding period in 2012.

The following shows the breakdown of net interest income according to main operating segment:

Segment	For the year ended 31 December		
	2013	2012	Change
	NIS millions		%
Households	**2,648**	2,799	(5.4)
Small businesses	**949**	924	2.7
Corporate banking	**1,384**	1,548	(10.6)
Commercial banking	**1,379**	1,391	(0.9)
Private banking	**293**	350	(16.3)
Financial management – capital markets	**692**	382	81.2
Other	**12**	14	(14.3)
Total	**7,357**	7,408	(0.7)

Total Interest Margin in 2013 was 2.08%, similar to the margin in 2012.

The interest margins in activity in Israel by segment were as follows:

In the unlinked shekel sector, 2.54%, compared to 2.59% in the corresponding period last year. The interest margin in the foreign currency sector was 1.77%, compared to 1.63% in the corresponding period last year. In the index-linked segment, the interest margin was 0.22%, compared 0.27% in the corresponding period last year.

For further information, see Management Review, Exhibit C and Note 20 to the financial statements.
For further details on the changes in the net interest income before expenses in respect of credit losses by sector, see Note 27(A) to the financial statements.

Expenses in respect of credit losses of Leumi Group amounted to NIS 268 million in 2013, compared with NIS 1,236 million in 2012, a decrease of 78.3%. In the Bank, expenses in respect of credit losses amounted to NIS 27 million in 2013, compared with NIS 1,069 million in 2012, a decrease of 97.5%.

The decrease in expenses in respect of credit losses derives from a decrease in the individual allowance in the Bank, which was partially offset by an increase in expenses in respect of credit losses in the Bank's overseas units in London and in the United States.

In the fourth quarter of 2013, expenses in respect of credit losses amounted to NIS 155 million, compared with NIS 386 million in the corresponding period last year.

Data on credit loss expenses (income) by quarter are as follows:

	2013					2012				
	Total 2013	**4th quarter**	3rd quarter	2nd quarter	1st quarter	Total 2012	4th quarter	3rd quarter	2nd quarter	1st quarter
	NIS millions									
Individual expense (income) in respect of credit losses	**11**	**59**	**(80)**	39	(7)	923	391	211	160	161
Collective expense (income) in respect of credit losses	**257**	**96**	**36**	45	80	313	(5)	81	173	64
Total expense (income) in respect of credit losses	**268**	**155**	**(44)**	84	73	1,236	386	292	333	225
Percentage ratios (in annual terms):										
Individual expenses in respect of credit losses to total credit to the public, net	**-**	**0.10**	**(0.13)**	0.07	(0.01)	0.38	0.65	0.35	0.27	0.26
Collective expenses in respect of credit losses to total credit to the public, net	**0.11**	**0.16**	**0.06**	0.08	0.13	0.13	(0.01)	0.13	0.29	0.11
Total expenses in respect of credit losses to total credit to the public, net	**0.11**	**0.26**	**(0.07)**	0.15	0.12	0.51	0.64	0.48	0.56	0.37
Individual expenses in respect of credit losses to total credit risk to the public	**-**	**0.06**	**(0.09)**	0.04	(0.01)	0.25	0.43	0.23	0.17	0.18
Collective expenses in respect of credit losses to total credit risk to the public	**0.07**	**0.10**	**0.04**	0.05	0.09	0.09	(0.01)	0.09	0.19	0.07
Total expenses in respect of credit losses to total credit risk to the public	**0.07**	**0.16**	**(0.05)**	0.09	0.08	0.34	0.42	0.32	0.36	0.25

The following table shows the balance of the allowance for credit losses on a collective basis:

	31 December 2013	31 December 2012
	NIS millions	
Allowance for credit losses on a collective basis (NIS in millions)	**2,702**	2,631
Allowance for credit losses on a collective basis as a percentage of total credit to the public, net (%)	**1.12**	1.09
Allowance for credit losses on a collective basis as a percentage of total credit risk to the public, net (%)	**0.72**	0.72

The following table shows the breakdown of expenses (income) in respect of credit losses according to principal operating segments:

	For the year ended 31 December 2013		For the year ended 31 December 2012	
	NIS millions	Percentages*	NIS millions	Percentages*
Households	**179**	**0.2**	71	0.1
Private banking	**9**	**0.1**	1	-
Small businesses	**112**	**0.5**	84	0.4
Corporate banking	**(166)**	**(0.3)**	933	1.3
Commercial banking	**186**	**0.4**	176	0.4
Financial management and other	**(52)**	**(9.1)**	(29)	(4.1)
Total	**268**	**0.11**	1,236	0.51

* Percentage of total credit at year end.

The following table shows the breakdown of expenses (income) in respect of credit losses by principal sectors of the economy:

	For the year ended 31 December	
	2013	2012
	NIS millions	
Agriculture	**(2)**	(10)
Industry	**93**	299
Construction and real-estate	**(21)**	103
Electricity and water	**(11)**	-
Trade	**(9)**	194
Hotels, accommodation and food	**14**	(59)
Transport and storage	**(28)**	52
Communications and computer services	**11**	(48)
Financial services	**(115)**	568
Other business services	**75**	15
Public and communal services	**23**	42
Private individuals – housing loans	**53**	(13)
Private individuals – other	**182**	93
Total - public	**265**	1,236
Total - banks	**3**	-
Total	**268**	1,236

The following table shows the breakdown of expenses (income) in respect of credit losses in the Group (the Bank and consolidated companies) that were recorded in the statement of profit and loss:

	For the year ended 31 December		
	2013	2012	Change
	NIS millions		%
The Bank	**27**	1,069	(97.5)
Arab Israel Bank	**9**	15	(40.0)
Leumi Mortgage Bank *	**-**	(10)	-
Leumi Card	**10**	19	(47.4)
Bank Leumi USA	**38**	26	46.2
Bank Leumi UK	**182**	108	68.5
Leumi Private Bank Switzerland	**-**	6	-
Leumi Romania	**1**	1	-
Leumi Tech Ltd. (formerly, Leumi Leasing and Investments)	**1**	2	(50.0)
Total expenses	**268**	1,236	(78.3)

* Activity merged with the Bank on 31 December 2012.

The following table shows the expenses in respect of credit losses as a percentage of the balance of credit to the public at the Bank's responsibility:

	2013	2012	2011	2010	2009	2008	2007	2006	2005	2004	2003
	%										
The banking system in Israel	0.26	0.41	0.38	0.40	0.73	0.71	0.21	0.52	0.69	0.88	1.13
Leumi Group	**0.11**	0.51	0.30	0.26	0.74	1.01	0.20	0.51	0.79	0.87	1.09

Problem credit risk

On a consolidated basis	**31 December 2013**		
	Balance sheet	Off- balance sheet	Total
	NIS millions		
1. Problem credit risk: (1)			
Impaired credit risk	**5,782**	**333**	**6,115**
Subordinate credit risk	**1,832**	**187**	**2,019**
Credit risk under special supervision (2)	**3,260**	**795**	**4,055**
Total problem credit	**10,874**	**1,315**	**12,189**
Of which: Unimpaired debts, in arrears of 90 days or more (2)	**1,440**	**-**	**-**
2. Noninterest-performing assets:			
Impaired debts	**5,218**	**-**	**-**
Assets received in respect of credit cleared	**101**	**-**	**-**
Total noninterest-performing assets	**5,319**	**-**	**-**

On a consolidated basis	31 December 2012		
	Balance sheet	Off- balance sheet	Total
	NIS millions		
1. Problem credit risk: (1)			
Impaired credit risk	7,458	515	7,973
Subordinate credit risk	2,050	109	2,159
Credit risk under special supervision (2)	2,779	664	3,443
Total problem credit	12,287	1,288	13,575
Of which: Unimpaired debts, in arrears of 90 days or more (2)	1,293	-	-
2. Noninterest-performing assets:			
Impaired debts	7,171	-	-
Assets received in respect of credit cleared	65	-	-
Total noninterest-performing assets	7,236	-	-

Note: Balance sheet and off-balance sheet credit risk is presented before the effect of the allowances for credit losses and before the effect of deductible collateral for the purpose of a borrower and a group of borrowers.

(1) Credit risk impaired risk, subordinate or under special supervision
(2) Including in respect of housing loans in respect of which there is an allowance according to the extent of arrears and in respect of housing loans in respect of which there is no allowance according to the extent of arrears which are in arrears of 90 days or more.

Below is a summary of credit risk indices:

	31 December 2013	31 December 2012
	%	
Balance of impaired credit to the public not accruing income as a percentage of the balance of credit to the public	**2.1**	2.8
Balance of credit to the public which is not impaired in arrears of 90 days or more as a percentage of the balance of credit to the public	**0.6**	0.5
Balance of the allowance for credit losses in respect of credit to the public as a percentage of the balance of credit to the public	**1.6**	1.7
Balance of the allowance for credit losses in respect of credit to the public as a percentage of the balance of impaired credit to the public not accruing interest income	**74.5**	60.6
Problem commercial credit risk in respect of the public as a percentage of total credit risk in respect of the public	**2.9**	3.3
Credit loss expenses as a percentage of the average balance of credit to the public (in annual terms)	**0.1**	0.5
Net write-offs in respect of credit to the public as a percentage of the average balance of credit to the public (in annual terms)	**0.2**	0.5
Net write-offs in respect of credit to the public as a percentage of the credit loss allowance in respect of credit to the public (in annual terms)	**13.2**	27.8

Noninterest income of Leumi Group in 2013 amounted to NIS 5,517 million, compared with NIS 4,774 million in the corresponding period last year, an increase of NIS 743 million, or 15.6%.

Noninterest income of the Bank in 2013 amounted to NIS 3,910 million, compared with NIS 3,265 million in the corresponding period last year, an increase of 19.8%.

In the fourth quarter of the year, non-interest income amounted to NIS 1,420 million, compared with NIS 1,394 million in the corresponding period last year, an increase of 1.9%.

The changes in non-interest income in the Group derive from:

	For the three months ended			For the year ended		
	31 December 2013	31 December 2012		**31 December 2013**	31 December 2012	
	NIS millions		% Change	NIS millions		% Change
Non-interest financial income	**238**	205	16.1	**1,127**	444	+
Commissions	**1,084**	1,107	(2.1)	**4,188**	4,199	(0.3)
Other income	**98**	82	19.5	**202**	131	54.2
Total	**1,420**	1,394	1.9	**5,517**	4,774	15.6

The following shows the quarterly development of noninterest income:

	2013				2012			
	4th quarter	3rd quarter	2nd quarter	1st quarter	4th quarter	3rd quarter	2nd quarter	1st quarter
	NIS millions							
Non-interest financial income	**238**	266	212	411	205	119	(25)	145
Commissions	**1,084**	1,050	1,029	1,025	1,107	1,050	1,022	1,020
Other income	**98**	66	5	33	82	39	(2)	12
Total	**1,420**	1,382	1,246	1,469	1,394	1,208	995	1,177

Details of non-interest financial income are as follows:

	For the year ended		
	31 December 2013	31 December 2012	Change
	NIS millions		%
Net income (expenses) in respect of derivative instruments and net exchange rate differences	**204**	(76)	+
Profits from sale of available-for-sale debentures, net	**209**	291	(28.2)
Profits (losses) from investments in shares including dividends *	**580**	(10)	+
Net profits in respect of loans sold	**99**	-	+
Realized and unrealized gains from adjustments of tradable debentures and shares to fair value, net	**35**	239	(85.4)
Total	**1,127**	444	+

* Including profit on the sale of shares of Migdal and Caesar Stone amounting to NIS 358 million and NIS 86 million (respectively) before the effect of tax in 2013 and the recording of an impairment of a nature other than temporary in respect of the investment in the shares of Partner Communication Ltd. amounting to NIS 160 million, net in 2012.

	For the three months ended		
	31 December 2013	31 December 2012	Change
	NIS millions		%
Net income (expenses) in respect of derivative instruments and net exchange rate differences	**73**	76	(3.9)
Profits from sale of available-for-sale debentures, net	**52**	28	85.7
Profits (losses) from investments in shares including dividends	**20**	13	53.8
Net profits in respect of loans sold	**6**	-	+
Realized and unrealized gains (losses) from adjustments of tradable debentures and shares to fair value, net	**87**	88	(1.1)
Total	**238**	205	16.1

The following table shows the development of the main items in noninterest financial income:

	2013				2012			
	4th quarter	3rd quarter	2nd quarter	1st quarter	4th quarter	3rd quarter	2nd quarter	1st quarter
	NIS millions							
Income (expenses), net, in respect of derivative instruments and net exchange rate differences	**73**	14	55	62	76	(98)	(157)	103
Profits from the sale of available-for-sale of debentures, net	**52**	34	24	99	28	137	68	58
Profits (losses) from investments in shares, including dividends	**20**	206	115	239	13	25	(34)	(14)
Profits in respect of loans sold	**6**	16	34	43	-	-	-	-
Realized and unrealized gains (losses) from adjustments of tradable debentures and shares to fair value, net	**87**	(4)	(16)	(32)	88	55	98	(2)
Total	**238**	266	212	411	205	119	(25)	145

Noninterest income was affected as follows:

In the first quarter of 2013, income on the sale of shares of Migdal amounting to NIS 180 million, before the effect of tax, was recorded, compared to an expense in respect of the impairment of the shares of Partner amounting to NIS 59 million in the corresponding period last year.

In the second quarter of 2013, income from the sale of shares in Caesar Stone amounting to NIS 86 million before the effect of tax was recorded, compared to an expense in respect of a decline in the value of shares in Partner amounting to NIS 101 million in the corresponding period last year.

In the third quarter of 2013, a profit on the sale of shares of Migdal amounting to NIS 163 million, before the effect of tax, was recorded, while in the corresponding period last year there were profits from the sale of available-for-sale debentures.

In the fourth quarter of 2013, the income was mainly due to net income in respect of derivative instruments and exchange rate differences and margins from tradable debentures – similar to the fourth quarter last year.

The following table presents a breakdown of commissions:

	For the year ended			
	31 December 2013	31 December 2012	Change	
	NIS millions		NIS millions	%
Account management	**833**	868	(35)	(4.0)
Activity in securities and derivative instruments	**817**	835	(18)	(2.2)
Credit cards	**907**	864	43	5.0
Dealing with credit	**332**	358	(26)	(7.3)
Financial product distribution commissions	**249**	227	22	9.7
Conversion differences	**289**	298	(9)	(3.0)
Commissions from financing transactions	**450**	425	25	5.9
Other commissions	**311**	324	(13)	(4.0)
Total commissions	**4,188**	4,199	(11)	(0.3)

In connection with legal claims and discussions with the Antitrust Commissioner on subjects related to credit cards, see Note 18(H) to the financial statements.
In connection with the notice of the Antitrust Commissioner regarding the adjustment of fees, see Note 18(J).

Income from commissions in 2013 was affected by various regulatory provisions and by the appreciation of the shekel against foreign currencies.

Income from commissions accounts for 46.9% of the operating and other expenses, compared with 46.1% in 2012.

Details of other income are as follows:

	For the year ended		
	31 December 2013	31 December 2012	Change
	NIS millions		%
Profits from severance pay fund	**129**	95	35.8
Other income	**73**	36	+
Total	**202**	131	54.2

In the item, profits from severance pay fund, income as a result of high yields in the employee severance pay funds were recorded in the third quarter and fourth quarter of 2013.

The development of non-interest income by main operating segment is as follows:

Segment	For the year ended		
	31 December 2013	31 December 2012	Change
	NIS millions		%
Households	**1,806**	1,852	(2.5)
Small businesses	**546**	507	7.7
Corporate banking	**646**	637	1.4
Commercial banking	**575**	556	3.4
Private banking	**610**	657	(7.2)
Financial management	**1,308**	600	+
Other	**26**	(35)	+
Total	**5,517**	4,774	15.6

The proportion of non-interest income from total income (i.e., net interest income and non-interest income) was 42.9%, compared with 39.2% in 2012.

Total operating and other expenses of Leumi Group in 2013 amounted to NIS 8,933 million, compared with NIS 9,100 million in 2012, a decrease of 1.8%. Total operating and other expenses of the Bank in 2013 amounted to NIS 6,913 million, compared with NIS 6,774 in 2012, an increase of 2.1%.

Operating and other expenses in the fourth quarter of 2013 amounted to NIS 2,254 million, compared with NIS 2,611 million in the corresponding period in 2012, a decrease of 13.7%.

Salary expenses in 2013 amounted to NIS 5,174 million, compared with NIS 5,290 million in 2012, a decrease of 2.2%

The decrease in salary expenses derives, inter alia, from the effect of a reduction in personnel as part of the streamlining program (see below in the chapter, "Human Resources"), which is spread over three years to the end of 2014, and includes streamlining in the number of personnel in the Bank and its subsidiaries in Israel and abroad. Hence, in 2012, a provision of NIS 323 million was made in respect of voluntary retirement, compared to only NIS 75 million in 2013. These effects were offset due to salary expenses in respect of current promotions in accordance with employment agreements in the Bank and for the provision for an annual return bonus.

The following table shows the quarterly development of salary expenses:

	2013					2012				
	Annual total	4th quarter	3rd quarter	2nd quarter	1st quarter	Annual total	4th quarter	3rd quarter	2nd quarter	1st quarter
	NIS millions									
Salary and fringe benefits	**4,039**	1,009	1,006	993	1,031	4,046	1,006	1,007	1,003	1,030
Return bonus	**367**	61	183	19	104	91	20	20	25	26
Pension expenses and severance pay, net of fund profits	**620**	186	141	146	147	744	(42)	328	328	130
Voluntary retirement	**75**	75	-	-	-	323	323	-	-	-
Regulatory changes	**73**	8	8	57	-	86	7	79	-	-
Total salary expenses	**5,174**	1,339	1,338	1,215	1,282	5,290	1,314	1,434	1,356	1,186

The changes in salary expenses were affected as follows:

In the first quarter of 2013, the total effect of an increase in employees' salaries was recorded with effect from 1 January. On the other hand, income from the severance pay funds and the remuneration fund was recorded throughout the year.

In the second quarter of 2013, there was an increase in pension provisions as a result of a decline in the profitability of the Bank employees' provident funds.

In the third quarter of 2013, there was an increase in the profitability of the provident and severance pay funds which reduced the provisions for pension and severance pay.

In the fourth quarter of 2013, there was an increase in salary expenses, due to carrying out actuarial changes and updating the actuarial model which led to an increase in liabilities.

Additional details on the components of salary expenses are as follows:

1. The Bank's actuarial obligation for pension and long-service grants in the financial statements are calculated using a capitalization rate of 4% determined by the Supervisor of Banks, and on the assumption of a real increase in salary based on past experience, and varying according to the age of the employee.

2. As a result of an increase in salary tax from 17% to 18%, with effect from 2 June 2013, the Bank increased the pension liability by NIS 53 million before tax. In 2012, salary tax increased from 16% to 17% with effect from 1 September 2012, and as a consequence, the Bank increased the pension liability by NIS 63 million.

For further details – see Note 15 to the financial statements.

Salary and related expenses (excluding early retirement expenses) account for some 57.1% of total operating expenses, compared with 54.6% in 2012.

Operating and other expenses, excluding salary, amounted to NIS 3,759 million in 2013, compared with NIS 3,810 million in 2012, a decrease of 1.3%.

Additional significant changes were as follows:

1. A reduction in other expenses amounting to NIS 97 million, mainly in respect of expenses that were or were likely to be incurred by the Group as a result of the investigations being carried out by the U.S. authorities regarding American customers.

2. In light of changes in regulations in the field of international private banking expenses around the world, and in Switzerland, in particular, which increase the cost of the service, and in light of the expected effect of these changes on Leumi Private Bank (formerly Bank Leumi Switzerland), the Bank provided for a one-time amortization of goodwill for 2013 of NIS 76 million.

3. A decrease in expenses in respect of professional services amounting to NIS 36 million or 11.2%

Computer expenses in the Group, presented in Note 25 to the statements, do not include the computer expenses in the Bank, which are included among all the other expenses, due to the fact that the Computer Unit Center is within the Bank. These computer expenses mainly include the expenses of subsidiaries that purchase computer services and/or out-sourcing costs.

For further information, see Notes 24 and 25 of the financial statements.

The following table shows the quarterly development of operating and other expenses and maintenance of buildings and equipment *:

	2013					2012				
	Annual total	4th quarter	3rd quarter	2nd quarter	1st quarter	Annual total	4th quarter	3rd quarter	2nd quarter	1st quarter
	NIS millions									
Depreciation	**768**	**179**	179	225	185	775	226	184	188	177
Maintenance of buildings and equipment	**1,065**	**273**	264	264	264	1,044	268	268	258	250
Other expenses and amortization of intangible assets	**1,926**	**463**	662	475	326	1,991	803	408	398	382
Total operating and other expenses	**3,759**	**915**	1,105	964	775	3,810	1,297	860	844	809

* Excluding salary

The changes in operating and other expenses (excluding salary) in the first, second and fourth quarters of the year were not material and were attributable to the fact that some of the expenses are not linear. On the other hand, in the third quarter of 2013, a provision was made for expenses that are likely to be incurred by the Group as a result of investigations being conducted by the U.S. authorities. In 2012, a provision was made on the subject in the fourth quarter of the year.

Operating expenses constitute 69.4% of total income, compared with 74.7% in 2012 and excluding the provision for early retirement and provisions in respect of the U.S. customers, 67.0%, compared with 68.8% in 2012.

Total operating and other expenses (in annual terms) constitute 2.39% of the total balance sheet, compared with 2.42% for 2012.

Profit before taxes of Leumi Group for 2013 amounted to NIS 3,673 million, compared with NIS 1,846 million in 2012, an increase of 99.0%. The Bank's profit before tax amounted to NIS 2,949 million in 2013, compared to NIS 760 million in 2012.

In the fourth quarter of 2013, pre-tax profit of Leumi Group amounted to NIS 821 million, compared with NIS 181 million in the corresponding period last year.

Provision for taxes on profit of Leumi Group for 2013 amounted to NIS 1,391 million, compared with NIS 811 million in 2012. The rate of the provision in 2013 was some 37.9% of the pre-tax profit, compared with 43.9% in 2012, a decrease of some 6.0 percentage points. The decrease in the rate of tax provision is primarily attributable to a reduction in disallowed expenses and in respect of a provision made last year for the impairment of an investment in a subsidiary.

Provision for tax

In the first quarter of the year, the tax rate was 42.1%, compared to 39.0% in the corresponding quarter in 2012. The increase in the rate of tax is mainly the result of negative exchange rate differences in respect of investments in foreign subsidiaries, compared to positive exchange rate differences in the corresponding period in 2012.

In the second quarter of the year, the tax rate was 34.5%, compared with 41.2% in the corresponding period last year, mainly due to a decrease in unrecognized expenses in respect of a provision made last year for a decline in the value of an investment in a subsidiary.

In the third quarter, the tax rate was 37.1%, compared to 22.9% in the corresponding period in 2012, mainly as a result of an increase in disallowed expenses compared to the corresponding period last year.

In the fourth quarter, the tax rate reached 36.4%, compared with 128.6% in the corresponding period last year, mainly due to a decrease in disallowed expenses and an increase in profit before tax in the quarter compared with the corresponding period last year.

Profit after taxes for 2013 amounted to NIS 2,282 million, compared with NIS 1,035 million in 2012, an increase of 120.5%. The profit after taxes for the fourth quarter of 2013 amounted to NIS 522 million, compared with a loss of NIS 52 million in corresponding period last year.

The Group share in the profit (loss) after taxes of companies included on equity basis amounted to a loss of NIS 293 million in 2013, compared with a loss of NIS 67 million in 2012. For details, see the section below, "Sectors of Activity within the Group" in the chapter, "Financial Management – Capital Markets".

Most of the loss in this item derives from the contribution of the following companies:

1. The Israel Corporation Ltd. – A loss of NIS 340 million in 2013 in 2013 compared with a loss a loss of NIS 110 million in 2012. For further details of a change in accounting policy, see chapter, "Operating segments, Activities in Products and Profit Centers of the Group, Companies Included on Equity Basis (non-bank)".

2. Companies included on equity basis of Leumi Partners Ltd. – a profit of NIS 35 million in 2013, compared with a profit of NIS 34 million in 2012.

Net profit before attribution to holders of non-controlling interests amounted to NIS 1,989 million in 2013, compared with a profit of NIS 968 million in 2012, an increase of 105.4%. In the fourth quarter of 2013, there was a loss before attribution to holders of non-controlling interests amounting to NIS 357 million, compared with a loss of NIS 251 million in the corresponding period in 2012.

Net profit attributable to holders of non-controlling interests in 2013 amounted to NIS 42 million, compared to a profit of NIS 37 million in 2012.

Net profit attributable to the shareholders of the banking corporation for 2013 amounted to NIS 1,947 million, compared with a profit of NIS 931 million in 2012, an increase of 109.1%. In the fourth quarter of 2013, there was a profit attributable to the shareholders of the banking corporation amounting to NIS 348 million, compared with a loss of NIS 259 million in the corresponding period in 2012.

Return on Equity – Average for the Period to Shareholders of the Banking Corporation in Annual Terms:

	2013					2012				
	Total 2013	**4th quarter**	3rd quarter	2nd quarter	1st quarter	Total 2012	4th quarter	3rd quarter	2nd quarter	1st quarter
	%									
Net profit (loss) attributable to the shareholders of the banking corporation	**7.6**	**5.4**	8.9	7.6	9.4	3.8	(4.0)	8.0	4.7	7.5

Total basic net profit per share attributable to the shareholders of the banking corporation in 2013 was NIS 1.32, compared to NIS 0.63 in 2012.

The following table presents a statement of total profit:

	For the year			
	2013	2012	Change	
	NIS millions		NIS millions	%
Net profit attributable to the shareholders of the banking corporation *	**1,947**	931	1,016	109.1
Other comprehensive income (loss) before tax *	**(622)**	1,012	(1,634)	-
Effect of tax attributable to other comprehensive income	**130**	(355)	485	+
Other comprehensive income attributable to noncontrolling interests	**3**	-	3	+
Total profit attributable to shareholders of the banking corporation	**1,458**	1,588	(130)	(8.2)

* The loss in the item, other comprehensive income, in 2013 is primarily attributable to the sale of shares from the available-for-sale shares in respect of which the profits have been classified to net profit attributable to shareholders in the banking corporation.

	For the three months ended			
	31 December 2013	31 December 2012	Change	
	NIS millions		NIS millions	%
Net profit (loss) attributable to the shareholders of the banking corporation	**348**	(259)	607	+
Other comprehensive income (loss) before tax	**(6)**	355	(361)	-
Effect of tax attributable to other comprehensive income	**(16)**	(187)	171	+
Other comprehensive income attributable to noncontrolling interests	**-**	2	(2)	-
Total profit attributable to shareholders of the banking corporation	**326**	(89)	415	+

Structure and Development of Assets and Liabilities

Total Assets of the Leumi Group on 31 December 2013 amounted to NIS 374.4 billion, compared with NIS 376.2 billion at the end of 2012, a decrease of 0.5%. The Bank's total assets on 31 December 2013 amounted to NIS 342.8 billion, compared with NIS 340.3 billion at the end of 2012, an increase of 0.7%.

Out of the Group's total assets, the value of assets denominated in or linked to foreign currency was some NIS 80.5 billion, some 21.5% of total assets. In 2013, the shekel appreciated against the US dollar by 7.0% and against the euro by 2.8%. The change in the exchange rates of the shekel against foreign currencies contributed to a decrease of 1.4% in the Group's total balance sheet, so that canceling the effect of the appreciation of the shekel, the total balance sheet was NIS 379.6 billion.

Total assets under the Group's management – The total balance sheet as well as customers' securities portfolios, and provident funds and supplementary training funds in relation to which operational management and deposit management services are provided – amounted to NIS 1,086 billion, compared with some NIS 989 billion at the end of 2012 (about US$ 313 billion and US$ 265 billion respectively).

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

	Consolidated			The Bank		
	31 December			31 December		
	2013	2012	Change	**2013**	2012	Change
	NIS millions		%	NIS millions		%
Total assets	**374,360**	376,160	(0.5)	**342,774**	340,309	0.7
Cash and deposits with banks	**44,351**	54,621	(18.8)	**40,413**	49,438	(18.3)
Securities	**63,735**	56,408	13.0	**57,203**	49,475	15.6
Credit to the public, net	**240,874**	241,264	(0.2)	**209,940**	207,922	1.0
Buildings and equipment	**3,638**	3,705	(1.8)	**3,131**	3,248	(3.6)
Deposits of the public	**286,003**	289,538	(1.2)	**273,186**	274,482	(0.5)
Deposits from banks	**4,310**	4,073	5.8	**7,522**	7,066	6.5
Debentures, notes and subordinated notes	**25,441**	27,525	(7.6)	**6,526**	6,822	(4.3)

B. The following table sets out the development of the main off-balance sheet items:

	Consolidated			The Bank		
	31 December			31 December		
	2013	2012	Change	**2013**	2012	Change
	NIS millions		%	NIS millions		%
Documentary credits	**1,863**	1,818	2.5	**1,278**	1,160	10.2
Credit guarantees	**5,406**	5,717	(5.4)	**4,483**	4,777	(6.2)
Guarantees to purchasers of apartments	**15,507**	13,520	14.7	**15,507**	13,520	14.7
Other guarantees and liabilities	**14,861**	16,283	(8.7)	**14,495**	15,813	(8.3)
Derivative instruments*	**539,651**	455,424	18.5	**530,833**	443,800	19.6
Options of all kinds	**130,980**	111,390	17.6	**130,321**	109,393	19.1

* Including "forward" transactions, financial swap contracts, swaps, futures and credit derivative transactions. For further details, see Note 18a and 18**f** to the financial statements.

C. The following table sets out the development of balances of customers' off-balance sheet financial assets with the Leumi Group [(1)]:

	2013	2012	Change
	NIS millions		%
Securities portfolios of customers	**604,095**	527,582	14.5
Of which: in the management of mutual funds (2) (3)	**78,590**	60,482	29.9
Provident funds (2) (3)	**66,533**	53,372	24.7
Supplementary training funds (2) (3)	**41,375**	32,747	28.6
Total	**712,003**	613,201	16.1

(1) Including a change in market value of securities and the value of securities of mutual and provident funds held in custody, in respect of which operational management and custodial services are provided.
(2) The Group in Israel does not manage mutual funds, provident funds or supplementary training funds.
(3) Assets of customers in relation to which the Group provides operational management services, including balances of the funds of customers who receive counseling at Leumi.

The increase in the value of the assets results from an increase in total activity and an increase in market values in Israel and abroad.

Deposits of the Public

Deposits of the public with the Group amounted to NIS 286.0 billion at the end of 2013, compared with NIS 289.5 billion at the end of 2012, a decrease of 1.2%.

The appreciation of the shekel against most foreign currencies contributed to a 2.2% decrease in total deposits of the public, so that after canceling the effect of the appreciation of the shekel, the increase in deposits of the public was 1.0%.

Debentures, notes and subordinated notes, the balance of which was some NIS 25.4 billion as at the end of 2013, compared with NIS 27.5 billion at the end of 2012. Deposits of the public, debentures and subordinated capital notes decreased in 2013 by 1.8%, and together constitute 83.2% of total assets.

The following table sets out the mix of deposits of the public by type and linkage sector:

	31 December 2013				
	On demand	Short-term	Savings schemes	Earmarked deposits	Total
	NIS millions				
Israeli currency:					
Unlinked	**43,250**	**111,573**	**-**	**2**	**154,825**
CPI-linked	**-**	**26,189**	**2,590**	**-**	**28,779**
Foreign currency:					
Including linked to foreign currency	**51,046**	**50,732**	**-**	**-**	**101,778**
Non-monetary	**-**	**621**	**-**	**-**	**621**
Total	**94,296**	**189,115**	**2,590**	**2**	**286,003**

	31 December 2012				
	On demand	Short-term	Savings schemes	Earmarked deposits	Total
	NIS millions				
Israeli currency:					
Unlinked	34,125	117,835	-	2	151,962
CPI-linked	-	25,786	2,677	4	28,467
Foreign currency:					
Including linked to foreign currency	41,230	67,541	-	-	108,771
Non-monetary	-	338	-	-	338
Total	75,355	211,500	2,677	6	289,538

Developments in the various types of deposits were as follows:

- Unlinked shekel deposits of the public increased by NIS 2.9 billion, 1.9%, compared with 31 December 2012.

- Deposits of the public denominated in or linked to foreign currency fell by NIS 7.0 billion, 6.4%, compared with 31 December 2012, and after offsetting the effect of the changes in the exchange rate of the shekel, these deposits fell by 0.5%. Deposits of the public with the foreign subsidiaries in 2013 decreased by some 11.2%, or about NIS 3.7 billion, a result of an appreciation of the shekel against the foreign currencies in which the subsidiaries operate.

- CPI-linked shekel deposits increased by NIS 312 million (1.1%) compared with 31 December 2012, mainly in term deposits.

The following table sets out the development of deposits of the public by principal operating segments:

	31 December 2013	31 December 2012	% change
Segment	NIS millions		
Households	**118,634**	128,194	(7.5)
Small businesses	**22,830**	19,666	16.1
Corporate banking	**22,816**	26,281	(13.2)
Commercial banking	**51,878**	50,108	3.5
Private banking	**34,794**	38,338	(9.2)
Financial management, capital markets and other*	**35,051**	26,951	30.1
Total	**286,003**	289,538	(1.2)

The following table sets out the quarterly development of deposits of the public by main operating segment:

	2013				2012			
	4th quarter	3rd quarter	2nd quarter	1st quarter	4th quarter	3rd quarter	2nd quarter	1st quarter
	NIS millions							
Households	**118,634**	120,059	121,693	124,320	128,194	133,435	131,402	129,856
Small businesses	**22,830**	21,928	21,052	19,730	19,666	18,950	18,466	17,833
Corporate banking	**22,816**	22,088	20,822	21,452	26,281	23,692	23,038	23,896
Commercial banking	**51,878**	49,036	47,840	49,420	50,108	48,973	48,780	46,805
Private banking	**34,794**	35,698	35,767	36,529	38,338	39,126	37,864	38,025
Financial management – capital markets and other *	**35,051**	31,030	28,274	27,369	26,951	21,053	20,884	21,227
Total	**286,003**	279,839	275,448	278,820	289,538	285,229	280,434	277,642

* Includes mainly deposits of institutional bodies.

Deposits from Governments amounted to some NIS 397 million at the end of 2013. These deposits include deposits from government sources that were made available to the banks in former years mainly for restructuring debts of the kibbutzim, and also deposits for granting housing loans to eligible members of the public.

In 2013, there was a decline of some NIS 54 million in deposits from governments.

This item also includes deposits of foreign governments in overseas subsidiaries, which amounted to some NIS 241 million at the end of 2013, compared with NIS 191 million at the end of 2012.

Deposits with banks and deposits from banks

A. Deposits with banks (central and commercial):

	31 December 2013		31 December 2012	
	Central banks	Commercial banks	Central banks	Commercial banks
	NIS millions			
Israeli currency:				
Unlinked	**27,147**	**1,074**	36,418	1,156
CPI-linked	**-**	**272**	-	277
Foreign currency including linked to foreign currency	**5,901**	**7,967**	4,691	9,940
Total deposits with banks	**33,048**	**9,313**	41,109	11,373

Total deposits with banks fell by 19.3%.

B. Deposits from banks (central and commercial):

	31 December 2013		31 December 2012	
	From central banks	From commercial banks	From central banks	From commercial banks
	NIS millions			
Israeli currency:				
Unlinked	**-**	**1,719**	-	1,694
CPI-linked	**-**	**117**	-	166
Foreign currency including linked to foreign currency	**32**	**2,442**	-	2,213
Total deposits from banks	**32**	**4,278**	-	4,073

By law, the Bank of Israel is permitted to provide loans to banking corporations against collateral. The Bank uses its deposits with the Bank of Israel for this purpose, as well as a pledge against its securities portfolio.

On 31 December 2013, deposits of the Group with the Bank of Israel amounted to NIS 27.7 billion, against which there were no loans from the Bank of Israel.

As may be seen from these tables, the liquidity position of the Group is extremely high, and the Group has net deposits with banks amounting to NIS 38.1 billion.

Credit to the public, net

Credit to the public in the Leumi Group at the end of 2013 amounted to NIS 240.9 billion, compared with NIS 241.3 billion at the end of 2012. In the Bank, NIS 209.9 billion compared to NIS 207.9 million at the end of 2012. Credit to the public constitutes 64.3% of total assets, compared with 64.1% at the end of 2012.

The appreciation of the shekel against most foreign currencies contributed to a decrease of 1.2% in total credit to the public. After canceling the effect of the appreciation, there was an increase of 1.0% in total credit to the public, so that canceling the effect of the appreciation of the shekel, the total balance sheet was NIS 243.7 billion.

As well as granting credit to the public, the Group invests in the securities of companies, including securities of holding companies of banks, amounting to NIS 12,807 million at the end of 2013, compared with NIS 11,171 million at the end of 2012. These investments also involve credit risk.

The following table sets out the quarterly development of credit to the public by linkage segment:

	2013				
	Year	**31 December**	30 September	30 June	31 March
Unlinked in NIS millions*	**146,907**	**146,907**	144,606	140,910	139,436
% increase (decrease)	**6.6**	**1.6**	2.6	1.1	1.2
CPI-linked in NIS millions	**53,544**	**53,544**	53,709	53,657	54,235
% increase (decrease)	**(2.4)**	**(0.3)**	0.1	(1.1)	(1.1)
Foreign currency including foreign currency-linked in NIS millions	**40,423**	**40,423**	42,577	43,916	44,943
% increase (decrease)	**(16.9)**	**(5.1)**	(3.0)	(2.3)	(7.6)
Total in NIS millions	**240,874**	**240,874**	240,892	238,483	238,614
% increase	**(0.2)**	**0.0**	1.0	(0.1)	(1.1)

* Including non-monetary items.

Total credit to the public by the Group in Israel amounted to some NIS 217 billion at the end of 2013, compared to NIS 215 billion at the end of 2012.

The following table sets out the mix of credit to the public by linkage segment:

	31 December 2013		31 December 2012		Change
	NIS millions	% of mix	NIS millions	% of mix	%
Unlinked*	**146,907**	**61**	137,794	57	6.6
CPI-linked	**53,544**	**22**	54,847	23	(2.4)
Foreign currency and linked to foreign currency	**40,423**	**17**	48,623	20	(16.9)
Total	**240,874**	**100**	241,264	100	(0.2)

* Including non-monetary items.

Credit to the public in unlinked shekels increased by NIS 9,113 million, or 6.6%, and index-linked credit to the public fell by NIS 1,303 million, or 2.4%. The decrease in foreign currency and foreign currency-linked credit to the public amounted to NIS 8,200 million, or 16.9%, and after neutralizing the effect of the changes in the exchange rate of the shekel, credit to the public in foreign currency and linked to foreign currency increased by 11%.

Total credit to the public that was offset deriving from deposits according to the extent of their collection amounted to NIS 5.1 billion in the Group. Some 74.9% of such credit is granted from government deposits according to the extent of their collection for financing the purchase of an apartment (housing loans).

The following table sets out the distribution of credit in foreign currency, including foreign currency-linked credit, by principal currency:

	31 December 2013	31 December 2012
	NIS millions	
US dollar	**27,213**	32,924
Euro	**6,020**	6,622
Other currencies	**7,190**	9,077
Total	**40,423**	48,623

The following table sets out the development of indebtedness to the construction and real estate segment:

	31 December 2013	31 December 2012	Change
	NIS millions		%
Balance sheet credit risk	**46,064**	48,578	(5.2)
Guarantees to apartment purchasers*	**6,514**	5,905	10.3
Other off-balance sheet credit risk	**25,768**	25,546	0.1
Total	**78,346**	80,029	(2.1)

* Weighted according to balance sheet value.

Total credit risk of the construction and real estate sector in Israel (according to the report by sector of the economy in Exhibit E to the Management Review) fell by 2.5% in 2013. The credit risk of the construction and real estate sector in Israel constitutes some 21.1% of total credit risk in Israel. However, in accordance with the rules laid down by the Bank of Israel for calculating the rate of financing by sector of the economy, total indebtedness in the sector at the Bank amounts to some 17.7% of total indebtedness in Israel. In 2013, there was no sectoral excess of credit, similar to the end of 2012.

The following table sets out the development of credit to the public by principal operating segment:

Segment	**31 December 2013**	31 December 2012	Change
	NIS millions		%
Households	**100,243**	90,492	10.8
Of which: Housing loans	**68,556**	61,998	10.6
Small businesses	**23,299**	21,733	7.2
Corporate banking	**60,646**	70,252	(13.7)
Commercial banking	**49,630**	49,908	(0.6)
Private banking	**6,455**	8,170	(21.0)
Financial management, capital markets and others	**601**	709	(15.2)
Total at end of period	**240,874**	241,264	(0.2)

Total business credit (commercial banking and corporate banking) decreased by 8.2% to NIS 110.3 billion in 2013. Total private credit (households, small businesses and private banking) increased by 8.0% to NIS 130.0 billion in 2013.

For further details of the development of credit and credit risks by sector of the economy, see Exhibit E to the Management Review

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

	2013				2012			
	4th quarter	3rd quarter	2nd quarter	1st quarter	4th quarter	3rd quarter	2nd quarter	1st quarter
End of period balances	NIS millions							
Households	**100,243**	98,272	95,289	92,469	90,492	89,084	86,128	84,039
Of which: Housing loans	**68,556**	67,221	65,239	63,214	61,998	60,888	58,699	56,811
Small businesses	**23,299**	23,131	22,593	22,116	21,733	21,014	20,819	20,207
Corporate banking	**60,646**	62,940	63,704	66,961	70,252	70,895	74,815	77,660
Commercial banking	**49,630**	49,112	49,627	48,636	49,908	51,088	49,834	49,257
Private banking	**6,455**	6,840	6,720	7,361	8,170	8,508	8,658	8,451
Financial management, capital markets and others	**601**	597	550	1,071	709	875	1,173	886
Total at end of period	**240,874**	240,892	238,483	238,614	241,264	241,464	241,427	240,500

Lien 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 lien in favor of the Bank of Israel on its rights to receive amounts and monetary shekel payments that are or will be payable to the Bank from time to time, from its customers who are corporations (established according to the laws of the State of Israel), that are not in arrears with their repayments to the Bank of loans received from the Bank, of which the average duration of the credit does not exceed three years, and were granted or will be granted to these customers by the Bank. The amount of the lien is equal to the total of the amounts to be secured by the debenture, from time to time, up to an aggregate of NIS 1.1 billion.

This lien secures funds that are required for the Bank's operations for purpose of its activities with the CLS (Continuous Link Settlement) Clearinghouse.

For further details, see below in "Lien on Securities" in this chapter.

Credit risk by economic sector

The following table sets out the development of overall credit risk to the public (1) by principal sector of the economy:

Sector of the economy	**31 December 2013** Overall credit risk to the public	Percentage of total	31 December 2012 Overall credit risk to the public	Percentage of total	Rate of change
	NIS millions	%	NIS millions	%	
Agriculture	**2,187**	**0.6**	2,124	0.6	3.0
Industry	**38,745**	**10.4**	44,066	12.0	(12.1)
Construction and real estate (2)	**78,346**	**20.8**	80,029	21.8	(2.1)
Electricity and water	**4,882**	**1.3**	3,683	1.0	32.6
Trade	**30,251**	**8.1**	31,261	8.5	(3.2)
Hotels, accommodation and food services	**4,824**	**1.3**	5,329	1.4	(9.5)
Transportation and storage	**6,296**	**1.7**	6,410	1.7	(1.8)
Communications and computer services	**5,681**	**1.5**	6,422	1.7	(11.5)
Financial services	**47,112**	**12.6**	43,510	11.8	8.3
Other business services	**11,253**	**3.0**	11,340	3.1	(0.8)
Public and community services	**9,569**	**2.6**	9,151	2.5	4.6
Private individuals - housing loans	**71,985**	**19.2**	65,439	17.8	10.0
Private individuals – other	**63,063**	**16.9**	59,100	16.1	6.7
Total	**374,194**	**100.0**	367,864	100.0	1.7

(1) Including off-balance sheet credit risk and investments of the public in debentures, and other assets in respect of derivative instruments.

(2) Including housing loans which have been extended to purchasing groups in the process of building amounting to NIS 1,175 million and off-balance sheet risk amounting to NIS 2,027 million, compared to NIS 1,067 million and NIS 2,164 million, respectively, as of 31 December 2012.

Below is a distribution of credit risk in the real estate and construction sector by principal operating area:

	31 December 2013 Balance sheet credit risk	Off-balance sheet credit risk	Total credit risk	31 December 2012 Balance sheet credit risk	Off-balance sheet credit risk	Total credit risk
	NIS millions					
Construction for trade and services	**4,423**	**2,028**	**6,451**	5,050	2,911	7,961
Construction for industry	**946**	**851**	**1,797**	850	394	1,244
Construction for housing	**7,053**	**17,977**	**25,030**	6,643	16,792	23,435
Income generating assets	**20,802**	**3,225**	**24,027**	23,281	2,649	25,930
Other	**12,840**	**8,201**	**21,041**	12,754	8,705	21,459
Total construction and real estate sector	**46,064**	**32,282**	**78,346**	48,578	31,451	80,029

See Exhibit E to the Management Review for further details as to the distribution of credit to the public by sector of the economy.
Part of the information set out below is "**forward-looking information**". For the meaning of this term, see the chapter, "General Environment and Effect of External Factors on Activities" in the section "Description of the Banking Corporation's Business and Forward-Looking Information in the Directors' Report" above.

Below is additional data on total credit:

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

Credit ceiling in NIS thousands		**31 December 2013** Percentage of total number of borrowers	Percentage of total balance sheet credit	Percentage of total off-balance sheet credit	31 December 2012 Percentage of total number of borrowers	Percentage of total balance sheet credit	Percentage of total off-balance sheet credit
From	To	%					
0	80	**80.8**	**7,.5**	**19.6**	83.5	6.3	19.3
80	600	**17.3**	**27.7**	**10.8**	13.8	18.4	10.8
600	1,200	**1.2**	**8.1**	**2.7**	1.7	10.6	2.8
1,200	2,000	**0.3**	**3.3**	**1.8**	0.5	5.1	1.9
2,000	8,000	**0.3**	**7.5**	**4.5**	0.4	8.9	5.2
8,000	20,000	**0.1**	**7.0**	**4.9**	0.1	7.2	4.9
20,000	40,000	**0.03**	**6.3**	**5.7**	0.04	7.1	6.4
40,000	200,000	**0.03**	**14.4**	**16.5**	0.03	15.8	18.0
200,000	800,000	*** 0.01**	**10.4**	**22.9**	* 0.01	12.7	22.7
Above 800,000		*** 0.001**	**7.8**	**10.6**	** 0.00	7.9	8.0
Total		**100.0**	**100.0**	**100.0**	100.0	100.0	100.0

* In 2013, 149 borrowers and in 2012, 158 borrowers

** In 2013, 21 borrowers and in 2012, 19 borrowers.

For further details about the distribution of credit by size, see Note 4C to the financial statements.

The following table sets out details of balances of credit to the public and off-balance sheet credit risk exceeding NIS 800 million per single borrower, based on a more detailed cross-section of credit size by economic sector as of 31 December 2013:

1. Credit risk by size of credit of the borrower as of 31 December 2013:

Credit ceiling in NIS millions		Number of borrowers Total	Of which, related parties	Balance sheet credit Total	Of which, related parties	Off-balance sheet credit Total	Of which, related parties
From	To				In NIS millions		
800	1,200	**9**	**1**	**6,564**	**955**	**2,188**	**-**
1,200	1,600	**5**	**-**	**4,382**	**-**	**2,539**	**-**
1,600	2,000	**2**	**-**	**519**	**-**	**2,795**	**-**
2,000	2,400	**3**	**-**	**2,607**	**-**	**3,777**	**-**
2,400	2,800	**1**	**-**	**2,376**	**-**	**41**	**-**
3,200	3,524	**1**	**-**	**2,941**	**-**	**583**	**-**
Total		**21**	**1**	**19,389**	**955**	**11,923**	**-**

Credit risk by size of credit of the borrower as of 31 December 2012:

Credit ceiling in NIS millions		Number of borrowers		Balance sheet credit		Off-balance sheet credit	
		Total	Of which, related parties	Total	Of which, related parties	Total	Of which, related parties
From	To				In NIS millions		
800	1,200	9	-	4,464	-	4,222	-
1,200	1,600	5	-	5,723	-	1,052	-
2,000	2,400	3	1	4,312	2,016	2,122	-
2,800	3,200	1	-	2,878	-	62	-
3,200	3,301	1	-	2,175	-	1,126	-
Total		19	1	19,552	2,016	8,584	-

2. Credit risk according to economic sectors as of 31 December 2013:

	Number of borrowers	Balance sheet credit	Off-balance sheet credit
	Total	Total	Total
		In NIS millions	
Industry	**3**	**2,257**	**3,327**
Construction and real estate	**6**	**4,214**	**3,051**
Public and community services	**1**	**735**	**200**
Communications and computer services	**1**	**2,376**	**41**
Financial services	**8**	**5,813**	**4,182**
Electricity and water	**1**	**2,941**	**583**
Trade	**1**	**1,053**	**539**
Total	**21**	**19,389**	**11,923**

Credit risk according to economic sectors as of 31 December 2012:

	Number of borrowers	Balance sheet credit	Off-balance sheet credit
	Total	Total	Total
		In NIS millions	
Industry	4	2,298	4,195
Construction and real estate	5	3,699	1,470
Public and community services	1	778	235
Communications and computer services	1	2,878	62
Financial services	6	6,515	1,279
Electricity and water	1	2,175	1,126
Trade	1	1,209	217
Total	19	19,552	8,584

All the related parties in the above tables are corporations in which the Bank holds less than 20% and which are not controlling shareholders of the Bank. There are no debts in the credit detailed in the above table in respect of which provisions credit loss expenses have been recorded.

3. As at 31 December 2013, the Group had no exposure to a group of borrowers whose indebtedness exceeds 15% of the Bank's capital (for capital adequacy purposes).

For further information on the subject of groups of borrowers, see chapter, " Exposure to Risk and Methods of Risk Management, below.

4. The aggregate indebtedness of large borrowers, groups of borrowers and banking groups of borrowers whose debt is exceeds 10% of the Bank's capital, constituted 14.7% of the Bank's capital at 31 December 2013, compared with the regulatory limit of 120% of the Bank's capital**.**

Problem debts

The risk of problem credit after individual and collective allowances is as follows:

	31 December 2013			31 December 2012		
	Balance sheet	Off-balance sheet	Total	Balance sheet	Off-balance sheet	Total
	In NIS millions					
Impaired debts	**4,267**	**213**	**4,480**	5,620	393	6,013
Substandard debts	**1,689**	**185**	**1,874**	1,647	102	1,749
Special mention debts	**2,691**	**756**	**3,447**	2,543	626	3,169
Total	**8,647**	**1,154**	**9,801**	9,810	1,121	10,931

Problem credit risk:

	31 December 2013	31 December 2012
	Problem credit risk	Problem credit risk
	In NIS millions	
Commercial problem credit risk	**10,858**	12,264
Retail problem credit risk	**1,331**	1,311
Total	**12,189**	13,575
Allowance for credit losses	**2,388**	2,644
Problem credit after allowance for credit losses	**9,801**	10,931

For additional information on problem credit, see note 4 to the financial statements and Exhibit E in the Management Review.

Credit to governments as at 31 December 2013 amounted to NIS 558 million, an increase of NIS 116 million, 26.2%, compared with 31 December 2012.

Securities

The Group’s investments in securities as at 31 December 2013 amounted to NIS 63.7 billion, compared with NIS 56.4 billion in 2012, an increase of 13.0%.

Securities in the Group are classified into two categories: securities for trading and available-for-sale securities.

Securities for trading are presented in the balance sheet at fair value, and the difference between fair value and adjusted cost is charged to the statement of profit and loss.
Available-for-sale securities are presented in the balance sheet at fair value, with the difference between fair value and adjusted cost presented as a separate item in shareholders' equity in other overall profit, called "adjustments for presentation of available-for-sale securities at fair value" less the related tax. Whenever the impairment is of a non-temporary nature, the difference is charged to the statement of profit and loss.

Method of calculating fair value

The fair value of Israeli securities is based mainly on prices quoted on the Tel-Aviv Stock Exchange and the fair value of foreign securities on prices received from external sources.

Debentures in Israel which are denominated in NIS and are not tradable have been revalued using a model, as there is no active market for these debentures.

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

	31 December 2013				
	Adjusted cost	Unrealized gains from adjustments to fair value	Unrealized losses from adjustments to fair value	Fair value	Balance sheet value
	NIS millions				
Debentures					
Available-for-sale	**49,854**	**401**	**(222)**	**50,033**	**50,033**
For trading	**9,740**	*** 76**	***(33)**	**9,783**	**9,783**
	59,594	**477**	**(255)**	**59,816**	**59,816**
Shares and funds					
Available-for-sale	**2,744**	**156**	**(72)**	**2,828**	**2,828**
For trading	**1,017**	*** 78**	*** (4)**	**1,091**	**1,091**
	3,761	**234**	**(76)**	**3,919**	**3,919**
Total securities	**63,355**	**711**	**(331)**	**63,735**	**63,735**

* Carried to profit and loss.

	31 December 2012				
	Adjusted cost	Unrealized gains from adjustments to fair value	Unrealized losses from adjustments to fair value	Fair value	Balance sheet value
	NIS millions				
Debentures					
Available-for-sale	42,260	576	(109)	42,727	42,727
For trading	11,092	* 236	* (13)	11,315	11,315
	53,352	812	(122)	54,042	54,042
Shares and funds					
Available-for-sale	1,726	453	(12)	2,167	2,167
For trading	189	* 11	* (1)	199	199
	1,915	464	(13)	2,366	2,366
Total securities	55,267	1,276	(135)	56,408	56,408

* Carried to profit and loss.

As at 31 December 2013, some 82.9% of the Group's *nostro* portfolio was classified as available-for-sale securities and some 17.1% as the trading portfolio. This classification allows for flexibility in the management of the securities portfolio. Some 6.1% of the value of the securities represents investments in shares of companies that are not presented on equity basis, but according to cost or to the market value of the shares traded on the stock exchange.

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

	2013	2012
	NIS millions	
Debentures redeemed and/or sold (available-for-sale)	**51,921**	44,392
Purchases of debentures available-for-sale	**59,468**	50,300
Net profit from investments in debentures:		
Interest income	**1,022**	1,253
Net profit from sale and from decrease in value of available-for-sale debentures	**209**	291
Profit realized and/or unrealized from adjustments to fair value of debentures for trading	**(54)**	229

The following table sets out details of the composition of investments in debentures by linkage types:

	31 December 2013			31 December 2012		
	Government of Israel	Foreign governments	Other companies	Government of Israel	Foreign governments	Other companies
	NIS millions					
Israeli currency:						
Unlinked	**34,086**	**-**	**237**	26,319	-	860
CPI-linked	**2,141**	**-**	**1,269**	3,441	-	1,320
Foreign currency including foreign currency-linked	**1,610**	**4,871**	**15,602**	2,218	6,765	13,119
Total debentures	**37,837**	**4,871**	*** 17,108**	31,978	6,765	* 15,299

* Of which NIS 998 million is subordinated debentures as at 31 December 2013 (NIS 1,272 million as at 31 December 2012).

In 2013, there was an increase of some NIS 5.8 billion, about 10.7% in Group investments in corporate debentures, including banks and financial institutions, mainly in Government of Israel debentures.
The portfolio of debentures is invested in government debentures, mainly of the Israeli and United States governments.

See Note 3 to the financial statements for further details.

The following table sets the value of securities according to the method of measurement in million of NIS:

	31 December 2013	31 December 2012
	NIS millions	
Securities traded on an active market	**45,164**	40,458
Securities at prices fixed according to external models	**15,539**	13,102
Securities according to quotations from the counterparty or at cost	**3,232**	2,848
Total	**63,735**	56,408

For further details of the accounting policy and the method of valuing the securities portfolio and the distinctions between a temporary impairment and that of a non-temporary nature, see the section "Accounting Policy on Critical Subjects" and note 3 to the financial statements.

Below is a table of details of investments in corporate debentures (not banks) only issued in Israel and abroad, by sector of the economy (available-for-sale and trading portfolio):

	31 December 2013		31 December 2012	
	Issued in Israel	Issued abroad	Issued in Israel	Issued abroad
Economy sector	NIS millions			
Agriculture	**-**	**4**	-	15
Industry	**60**	**766**	179	801
Construction and real estate	**50**	**171**	53	244
Electricity and water	**590**	**234**	867	206
Trade	**186**	**4**	312	50
Transportation and storage	**9**	**132**	24	11
Communications and computer services	**58**	**198**	53	205
Financial services *	**431**	**9,495**	474	7,343
Business and other services	**66**	**209**	95	101
Public and community services	**29**	**115**	24	114
Total	**1,479**	**11,328**	2,081	9,090

* Including asset-backed securities.

The Available-for-Sale Portfolio

The following table shows the composition of the available-for-sale portfolio as at 31 December:

	2013		2012		Change	
	NIS millions					
	Abroad	In Israel	Abroad	In Israel	Abroad	In Israel
Debentures	**19,953**	**30,080**	20,400	22,327	(447)	7,753
Shares and funds	**1,741**	**1,087**	594	1,573	1,147	(486)
Total	**21,694**	**31,167**	20,994	23,900	700	7,267

a. In 2013, there was a negative change in other comprehensive income in respect of available-for-sale securities amounting to NIS 518 million (before the effect of tax). The change was attributable to a negative change in securities sold and classified to profit and loss amounting to NIS 747 million, which was partially offset from an increase in value amounting to NIS 229 million (before tax), This compared with an increase in value amounting to NIS 1,268 million (before tax). In the corresponding period last year, the negative change was attributable to securities sold and classified to profit and loss amounting to NIS 201 million (before tax).

b. In addition, NIS 209 million was recorded to profit and loss, in respect of net profits from the sale of available-for-sale debentures, compared with profits of NIS 291million in 2012**.**

c. The following table shows a summary of the above results in respect of the available-for-sale portfolio (including interest income):

	For the year ended	
	31 December 2013	31 December 2012
	NIS millions	
Profits in respect of available-for-sale securities which were recorded to profit and loss	**1,561**	1,167
Adjustments to capital reserve of available-for sale securities in shareholders' equity	**(518)**	1,067
Total change in respect of available-for-sale securities	**1,043**	2,234

d. The following table shows net balances in shareholders' equity:

	31 December 2013	30 September 2013	31 December 2012	Movement 4th Quarter	Movement Year 2013
	NIS millions				
Shares	**83**	66	441	17	(358)
Israel government debentures	**145**	125	150	20	(5)
Foreign government debentures	**2**	2	7	-	(5)
Other debentures	**(25)**	(1)	127	(24)	(152)
Lending of securities and capital reserve in respect of company included on equity basis	**18**	15	16	3	2
Total	**223**	207	741	16	(518)
Related tax	**(44)**	(44)	(247)	-	203
Net total	**179**	163	494	16	(315)

The accumulated net balance of adjustments to fair value of securities held in the available-for-sale portfolio, as at 31 December 2013, amounted to a positive amount of NIS 179 million (after the effect of tax) compared with a positive amount of NIS 494 million at the end of 2012. These amounts represent net profits which had not been realized at the dates of the financial statements.

Bank management estimates that there is impairment in securities in the available-for-sale portfolio, which is of a temporary nature. The Banks intends and is able to continue holding the investments until the expected recovery of the full cost of the assets or until their redemption. Accordingly, this impairment is recorded in capital. This is on the basis of the criteria set forth in note 1 to the financial statements "Significant Accounting Policies", below.

e. Below is the impairment in available-for-sale securities charged to shareholders' equity as at 31 December 2013:

		Duration of impairment since commencement of the impairment *				
		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	**12**	**13**	**-**	**-**	**25**
	Asset-backed debentures	**12**	**64**	**54**	**32**	**162**
	Other debentures	**20**	**18**	**-**	**15**	**53**
	Total	**44**	**95**	**54**	**47**	**240**
Above 10%	Shares	**26**	**21**	**-**	**-**	**47**
	Asset-backed debentures	**-**	**-**	**-**	**-**	**-**
	Other debentures	**-**	**-**	**-**	**7**	**7**
	Total	**26**	**21**	**-**	**7**	**54**
Total amount	Shares	**38**	**34**	**-**	**-**	**72**
	Asset-backed debentures	**12**	**64**	**54**	**32**	**162**
	Other debentures	**20**	**18**	**-**	**22**	**60**
Overall total		**70**	**116**	**54**	**54**	**294**

For the treatment of the evaluation of securities and distinctions between an impairment of a temporary nature and that of a non-temporary nature, see the chapter, "Accounting Policy on Critical Matters".
For further information, see below note 3 to the financial statements – Securities.

* The duration of the impairment from the commencement of the impairment means from the beginning of any impairment whatsoever of the security from the price of the adjusted cost.

Trading Portfolio

The following table shows the composition of the trading portfolio as at 31 December:

	2013		2012		Change	
	NIS millions					
	Abroad	In Israel	Abroad	In Israel	Abroad	In Israel
Debentures	**1,951**	**7,832**	1,635	9,680	316	(1,848)
Shares and funds	**959**	**132**	27	172	932	(40)
Total	**2,910**	**7,964**	1,662	9,852	1,248	(1,888)

In respect of trading debentures, realized and unrealized losses amounting to NIS (54) million were recorded in the statement of profit and loss, compared with profits amounting to NIS 229 million in 2012, and in respect of shares and funds, realized and unrealized profits were recorded amounting to NIS 89 million, compared with profits of NIS 10 million in 2012.

Investments in Securities Issued Abroad

The Group’s securities portfolio includes some NIS 25 billion (some US$ 7.2 billion) of securities issued abroad, all of which (except for some 1.6%) are investment grade securities, of which some 82% are rated 'A-' and above. Some 10% of the portfolio is invested in shares and funds. Of the said portfolio, some NIS 22 billion (some US$ 6.3 billion) is classified in the available-for-sale securities portfolio, and the balance is classified in the trading portfolio.

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

	2013		2012	
	Available-for-sale portfolio	Trading portfolio	Available-for-sale portfolio	Trading portfolio
Balance sheet value	NIS millions			
Government debentures*	**5,325**	**1,036**	8,487	447
Debentures of banks and financial institutions	**5,280**	**116**	5,281	88
Asset-backed debentures	**7,346**	**279**	5,049	358
Other debentures	**2,002**	**520**	1,583	742
Shares and funds	**1,741**	**959**	594	27
Total	**21,694**	**2,910**	20,994	1,662

* Of which Government of Israel debentures issued abroad at 31 December 2013, NIS 1,482 million in the available portfolio and NIS 8 million in the trading portfolio, and at 31 December 2012, NIS 2,033 million in the available portfolio and NIS 136 million in the trading portfolio.

The net impairment (the offset of costs and impairments) carried to capital in respect of securities issued abroad as at 31 December 2013 amounts to NIS (11) million (NIS 7 million after tax).

1. Asset-backed investments in securities issued abroad

The Group's asset-backed securities portfolio (both mortgage-backed and non-mortgage-backed), all of which is rated investment grade at 31 December 2013, amounted to NIS 7.6 billion (some US$ 2.2 billion), compared with NIS 5.4 billion at 31 December 2012. Of the said portfolio, some NIS 7.3 billion (some US$ 2.1 billion) is classified in the available-for-sale portfolio.

The available-for-sale portfolio of investments in asset-backed securities abroad as at 31 December 2013 includes an investment in mortgage-backed debentures amounting to NIS 5.5 billion. 94%of the total mortgage-backed debentures in the available-for-sale portfolio were issued by federal agencies in the United States (GNMA, FHLMC and FNMA).

The following table shows a summary of investments in asset-backed debentures in the available-for-sale portfolio:

	31 December 2013			
	Adjusted cost	Unrealized profits	Unrealized losses	Balance sheet value (fair value)
	NIS millions			
MBS - mortgage-backed securities	**5,673**	**7**	**(149)**	**5,531**
ABS asset-backed securities (other than mortgage-backed)	**1,801**	**27**	**(13)**	**1,815**
Of which: CLO	**1,709**	**27**	**(12)**	**1,724**
Other	**92**	**-**	**(1)**	**91**
Total	**7,474**	**34**	**(162)**	**7,346**

	31 December 2012			
	Adjusted cost	Unrealized profits	Unrealized losses	Balance sheet value (fair value)
	NIS millions			
MBS - mortgage-backed securities	3,611	22	(2)	3,631
ABS asset-backed securities (other than mortgage-backed)	1,382	54	(18)	1,418
Of which: CLO	1,334	54	(17)	1,371
Other	48	-	(1)	47
Total	4,993	76	(20)	5,049

For the definition of asset-backed securities see Note 3 to the financial statements.

Securitization Exposures

Investment in asset-backed securities by exposure type (Table 9(f) – Basel II):

	31 December 2013	31 December 2012
	Accrued amount of exposure	
	NIS millions	
Mortgage-backed securities (MBS):		
Pass-through securities:		
Securities guaranteed by US Government GNMA	**232**	257
Securities issued by FNMA and FHLMC	**1,581**	511
Other securities	**4**	5
Other mortgage-backed securities		
Securities issued by FHLMC, FNMA, or GNMA, or guaranteed by these entities	**3,374**	2,581
Other mortgage-backed securities	**428**	322
Total mortgage-backed securities (MBS)	**5,619**	3,676
Asset-backed securities (ABS):		
Credit card debtors	**85**	75
Lines of credit for any purpose secured by dwelling	**2**	5
Credit for purchase of vehicle	**57**	166
Other credit to private persons	**19**	20
Credit not to private persons	**1**	1
CLO debentures	**1,724**	1,371
Others	**118**	93
Total asset-backed (ABS)	**2,006**	1,731
Total asset-backed securities	**7,625**	5,407

Investment in asset-backed securities by risk weighting - available portfolio (Table 9(g) – Basel II)*

	31 December 2013	31 December 2012	**31 December 2013**	31 December 2012
	Accrued amount of exposure		Capital requirement for securitization exposure	
	NIS millions			
20%	**1,291**	727	**23**	13
40%	**321**	390	**12**	14
50%	**305**	169	**14**	8
100%	**224**	370	**20**	33
225%	**30**	42	**6**	8
350%	**-**	-	**-**	-
650%	**-**	2	**-**	1
Deducted from equity	**-**	21	**-**	-
Total	**2,171**	1,721	**75**	77

* From 31 December 2013, the Bank applies the Bank of Israel directives regarding re-securitization.
Not including, FNMA, FHLMC securities, which are presented as a U.S. Government obligation and the weight of their saving is 20%.
Not including GNMA securities for which there is U.S. State guarantee and the weight of their saving is 0%.

As at 31 December 2013, the accumulated net impairment charged to shareholders' equity resulting from the mortgage-backed securities portfolio was some NIS 142 million.

The projected term to maturity for all the mortgage-backed securities portfolio is an average of 5 years.

The total of the asset-backed debentures, which are not in the U.S. State guarantee and are not covered by U.S. federal institutions in the available-for-sale portfolio and the trading portfolio, amounts to some NIS 432 million.

In addition to mortgage-backed securities, the Group's available-for-sale portfolio also includes other securities backed by assets other than mortgages (car financing credit and other types of credit), amounting to some NIS 1.8 billion. Of these, CLO-type debentures amount to NIS 1.7 billion. The projected term to maturity of the portfolio of securities backed by assets other than mortgages is an average of 2.8 years.

The charge to profit and loss in respect of these two portfolios was made on the basis of the policy detailed in the section on Significant Accounting Policies in note 1 to the financial statements and in the chapter, "Accounting Policy on Critical Matters"

For the definition of asset-backed securities see note 3 to the financial statements.

2. Investments in other securities issued abroad (non asset-backed)

The Group's securities portfolio as at 31 December 2013 includes some NIS 17.0 billion (US$ 4.9 billion) of non-asset-backed securities. Of these securities, NIS 14.3 billion (US$ 4.1 billion) are classified in the available-for-sale portfolio, with the balance in the trading portfolio. Of the total securities, 95% are investment grade and they include mainly securities issued by the U.S. government, banks and financial institutions, securities, and the balance, mainly securities issued by the Israeli government.

For further details regarding exposure to overseas financial institutions, see chapter, "Exposure to Risk and Methods of Risk Management", in the section, "Credit Risk".

As at 31 December 2013, aggregate increase in value in shareholders' equity in respect of non-asset-backed securities issued abroad in the available-for-sale portfolio amounted to NIS 117 million (NIS 75 million after tax).

As stated above, in addition to the available-for-sale portfolio, the securities portfolio also includes non-asset backed securities in the trading portfolio. This includes mainly securities of states, banks and financial institutions, and securities funds. 95% of the securities in the trading portfolio are of investment grade.

The value of the non-asset backed trading portfolio as of 31 December 2013 amounted to NIS 2.6 billion (US$ 0.8 billion). The difference between fair value and adjusted cost, if there is such a difference, is recorded in the profit and loss account.

3. Investments in corporate debentures issued in Israel

Investments in debentures issued in Israel amounted to NIS 37.9 billion on 31 December 2013, of which NIS 36.4 billion was in debentures issued by the Government of Israel in NIS, with the balance in debentures of the Government of Israel in foreign currency and debentures issued by companies. Some 52.9% of the investments in corporate debentures amounting to some NIS 1.2 billion were included in the available-for-sale portfolio, and the balance was in the trading portfolio.

Corporate debentures in the available-for-sale portfolio amounting to NIS 1.2 billion includes a positive capital reserve amounting to NIS 45 million and a negative capital reserve amounting to NIS 2 million.

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. The revaluation of the traded corporate debentures is based on market prices on the stock exchange, and the revaluation of the non-listed corporate debentures is carried out as described above.

4. Investments in shares and funds

Total investments in shares and funds amounted to some NIS 3,919 million on 31 December 2013, of which NIS 2,556 million was in listed shares and NIS 1,363 million was in non-listed shares. Of the total investment, NIS 2,828 million is classified in the available-for-sale portfolio and NIS 1,091 million is classified in the trading portfolio.

Risk Management objectives and policy with regard to investment in shares - (Qualitative Disclosure – Table 13 - Basel II):

Investment policy:

The Bank has defined the Group's investment policy to include setting limits for the volume of overall investment and in a single company, the investment mix, and the various levels of risk between types of non-banking investments.

Definition of the aim of the investment:

- Achieving a higher return in comparison with a *nostro* financial investment.
- Maximizing the value of the investment and achieving better investment terms by leveraging the reputation of the Leumi Group.
- Widening the spread of risk and varying the Group's sources of revenue.
- Moderating the volatility of the *nostro* portfolio (time gaps).

The structure of the portfolio is divided into 3 sub-groups:

- Strategic investments (majority of the portfolio) which the Bank plans to hold for the long term
- Medium-term investments
- Investments in growth companies (start-up companies)

Accounting treatment of investments:

- Investments are recorded as investments in the available-for-sale securities portfolio. When the investment is in a company included on equity basis, it is recorded in "investments included on equity basis".

- With regard to the accounting method, see below in the financial statements, note 1F, Significant Accounting Policies.

The following table sets out the principal investments in shares and funds recorded in the securities item (1) (Table 13 (B) Basel II):

	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*		Capital adequacy requirement		Listed/not listed
	31 December 2013	31 December 2012	**31 December 2013**	31 December 2012	**31 December 2013**	31 December 2012	
	%		NIS millions				
Migdal Insurance and Financial Holdings Ltd.	**-**	9.79	**-**	594	**-**	53	listed
Africa Israel Properties Ltd.	**-**	2.22	**-**	22	**-**	2	listed
Otsar Hityashvuth HaYehudim B.M.	**8.62**	8.62	**61**	50	**5**	5	listed
Partner Communications Ltd. (2)	**2.90**	4.99	**146**	174	**13**	16	listed
Electra Consumer Products (1970) Ltd. (3)	**8.98**	8.98	**91**	57	**8**	5	listed
T.S.I. Roads Limited Partnership	**18.90**	17.82	**252**	108	**23**	10	not listed
Tower Semiconductor capital notes	**-**	-	**30**	49	**3**	4	not listed
Tower Semiconductor	**-**	-	**20**	-	**2**	-	listed
CLS Bank	**-**	-	**28**	21	**3**	2	not listed
Funds	**-**	-	**1,807**	825	**163**	74	674 not listed
Apax	**-**	-	**83**	72	**7**	6	not listed
Others	**-**	-	**1,401**	394	**126**	36	379 not listed
Total	**-**		**3,919**	2,366	**353**	213	

* The value of the investment in the consolidated balance sheet equals the balance of fair value of the investment.

(1) For details of non-banking investments reported on equity basis, see chapter, "Operating segments, Activities in Products and Profit Centers in the Group" below.

(2) Sold in March 2014 for NIS 140 million. The profit before tax was NIS 70 million.

(3) Sold in January 2014 for NIS 83.8 million. The profit before tax was NIS 17 million.

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

	Balance sheet amount	
	2013	2012
Shares and funds on basis of quoted prices in active market	**2,556**	1,172
Funds according to quote by counterparty	**757**	696
Unquoted shares on cost basis	**606**	498
Total	**3,919**	2,366

TSI Roads Limited Partnership

In July 2013, TSI Roads Limited Partnership ("the Partnership") purchased from Housing and Construction Ltd. its entire holdings in Derech Eretz (25.5% in full dilution). Prior to the transaction, the Partnership held 25.5% of the share capital of Derech Eretz and after the sale, 51% and is a controlling shareholder. Leumi Partners, which holds as a limited partner in the Partnership 18.91% of the rights in the Partnership invested for the purpose of the acquisition NIS 143 million and undertook to make a further investment in the Partnership, as long as the bank guarantees, issued in connection with Project are not realized, an additional amount of up to NIS 61 million,

Migdal

At the beginning of 2013, Leumi distributed some 5.08% of the shares of the company to a number of institutional entities at a price of NIS 5.72 per share (some 2.2% discount on the market price) and for aggregate consideration of NIS 306 million. As a result of the sale, the Bank recorded a net profit of NIS 120 million in the financial statements for the first quarter of 2013.

On 30 September 2013, Leumi distributed some 4.35% of the shares of the company to a number of institutional entities at a price of NIS 5.9 per share and for aggregate consideration of NIS 270 million. As a result of the sale, in the statements for the third quarter of 2013, the Bank recorded a net profit of NIS 105 million.

Securities Lien

The Bank is a member of the Stock Exchange Clearing House Ltd. and of the Ma'of Clearing House Ltd.

The Bank, like all other Ma'of Clearing House members, pledges securities from the *nostro* to secure its customers' activities, the *nostro* activities and its part of the risks fund. The pledge also secures amounts due in respect of obligations of the other members of the risks fund, if the pledge provided by another member is not sufficient to cover all his obligations and in proportion to the relevant share of each of the members of the fund, up to the lower of the amount of the collateral provided or the amount of the sums due to the Maof Clearing House. As at 31 December 2013, the Bank had pledged debentures with a value of NIS 983 million to the Maof Clearing House.

A similar collateral arrangement exists with the Stock Exchange Clearing House. The total value of debentures pledged by the Bank to the Stock Exchange Clearing House as at 31 December 2013 was NIS 80 million.

The Bank has signed a debenture in favor of the Bank of Israel as security for amounts due or that will be due to the Bank of Israel from the Bank. As collateral for the above, the Bank created a floating charge in favor of the Bank of Israel, unlimited in amount, over debentures deposited in a specific account maintained at the Tel Aviv Stock Exchange Clearing House in the name of the Bank of Israel. As at 31 December 2013 there were no balances outstanding.

As at 31 December 2013, the Bank had not been granted any loans from the Bank of Israel while the balance of the Bank's deposits with the Bank of Israel amounted to NIS 27.1 billion.

The Bank is executing short-term lending of securities in foreign currency from the available portfolio, via the Euroclear clearinghouse, for other customers of the clearinghouse, without knowing the identity of the borrowers. The lending is carried out under a full guarantee of the Euroclear clearinghouse which is an AA+ rated financial institution. The value of the balance of the securities lent to the Euroclear clearinghouse as of 31 December 2013 stood at some NIS 84 million. In order to guarantee clearance of securities for customers, the Bank received from the Euroclear Clearinghouse a credit line amounting to US$ 150 million, against which there is a floating lien of securities in the *nostro* portfolio.

Other assets and debit balances in respect of derivative instruments

At the end of 2013, other assets amounted to NIS 5.0 billion, compared with NIS 4.5 billion at the end of 2012, an increase of some 10.4%,

The balance of the fair value of derivative instruments made with and for customers rose from NIS 11.4 billion at 31 December 2012 to NIS 13.1 billion at 31 December 2013.

Other liabilities and credit balances in respect of derivative instruments

Other liabilities amounted to NIS 17.3 billion at 31 December 2013, compared with NIS 15.6 billion at 31 December 2012, an increase of 11.3%.

Credit balances in respect of derivative instruments amounted to NIS 13.5 billion at 31 December 2013, compared with NIS 12.8 billion at 31 December 2012.

Fixed Assets and Plant

Buildings and equipment - the amortized cost of buildings and equipment as at 31 December 2013 amounted to NIS 3.6 billion, compared to NIS 3.7 billion as at 31 December 2012.

Investments in buildings and equipment as at 31 December 2013 are as follows:

	Cost	Accumulated depreciation	Net book value	
			31 December 2013	31 December 2012
	NIS millions			
Buildings and land	**3,422**	**1,881**	**1,541**	1,559
Equipment, furniture and vehicles	**3,394**	**2,694**	**700**	712
Software	**4,978**	**3,581**	**1,397**	1,434
Total	**11,794**	**8,156**	**3,638**	3,705

The above buildings and equipment are used mainly for the activities of the Group. Buildings that are not used by the Group and are leased to non-Group parties are included in the consolidated balance sheet as at 31 December 2013 amounted to NIS 26 million.

The majority of the premises in which the business of the Group is conducted in Israel are owned by the Bank or by subsidiaries. Most of the properties in which the business of the Group is conducted abroad are leased.

Real estate assets of the Bank are held by the Bank, Binyanei Bank Ltd. and Lyn City Center Ltd. (wholly-owned subsidiaries of the Bank) and they own 166 properties, of which 121 are branches and archives and 23 are Head Office buildings. The total area under ownership is some 259,000 sq. mtrs., divided into branches - some 78,000 sq. mtrs., Head Office buildings (excluding the Bank Leumi Service Center complex in North Lod) – some 42,000 sq. mtrs., and the balance, divided amongst offices in use by subsidiaries, a logistical center, plots, vacant properties etc. Properties designated for sale constituted 16772 sq. mtrs. as of 31 December 2013, and are presented at the lower of amortized cost or realization value.

Investment in buildings owned by the Group in 2013 amounted to NIS 1,541 million (including property purchases amounting to NIS 70 million) compared with NIS 1,599 million in 2012 (including property purchases of NIS 70 million). In addition to areas owned by the Bank, the Bank holds leased property covering 83,000 sq. mtrs.

"Keshev" – "The Yitzhak Rabin Bank Leumi Service Center", which includes "Hatam" – the Operations and Computerized Operating Services Division of the Bank, the Procurement, Building and Logistics Department, and the Bank's training center, is located in Lod, within a facility comprising a total area of 78.8 dunams.

Leumi has established an underground facility for the computer complex. The facility is protected against rocket attack, biological and chemical warfare and earthquakes. The facility is constructed with advanced technology enabling high-level day-to-day operation and independent functioning in times of emergency. The transfer of the computer system to the facility was completed at the end of 2010. The infrastructure in the new computer center has an optimal survival and redundancy level and the structure is built in accordance with international standards.

Leumi has 2 mainframe computers produced by IBM, part of the Z Series range. For use by the production systems: a primary computer with an operating power of some 10,609 mips, with a current operating capacity of 9,788 mips (number of instructions in millions per second) and a secondary computer with an operating power of some 471 mips. The secondary production computer is expandable to a capacity of some 9,894 mips for internal back-up purposes in the Keshev facility.

One computer, with an operating power of some 2,147 mips, operates at the Tel Aviv facility, and serves as the development and testing environment. This computer is expandable to a capacity of some 13,662 mips in emergency situations in which the Keshev facility ceases to operate. A reexamination of the effectiveness of using the facility in Tel Aviv as a backup facility is planned to be carried out.

The Bank has an online and historical database stored on discs and cassettes in the main computer facility at Keshev and in the back-up facility in Tel-Aviv. A third up-to-date copy of data is stored in an installation in the Jerusalem area. The data go through designated communication infrastructure between Leumi's Computer Centers.

Leumi's branches are computerized and connected on-line to the Bank's computer center at Keshev. In the past year, the branches' servers were transferred to the Computer Center in Keshev and Tel Aviv. In total, 393 servers (of which 50 are in the Arab Israel Bank) and 7,865 work-stations (of which 487 are in the Arab Israel Bank), most of which are PC-based, have been installed in the branches. There are 357 innovative automatic teller machines, of which 194 include an option for depositing cash for use by customers and some 565 self-service "Leumi Digital" stations. At head office and district management units there are 12,200 personal computers (of which, 512 are in the Arab Israel Bank) connected in local area networks, with the capability of communicating directly with the computer center and have a separate external Internet connection.

During the years 2008-2012, the Bank upgraded the network of "Leumi Digital" customer stations and the process of replacing all of the customer stations with new and advanced equipment was completed.

As of the end of 2013, there were 223 Leumi Digital external customer stations and 342 internal customer stations.

In 2013, 61 old (10-20 years old) ATMs were replaced and new processers in some 60 other ATMs were upgraded. In addition, cheque deposit facilities were installed in some 50 ATMs.

Information security at Leumi is based on the principle of banking secrecy and various laws and directives, such as the provisions of the Protection of Privacy Law and related regulations, the provisions of the Computers Law, directives of the Bank of Israel, including Information Technology Management Directive 357, and accepted standards of information security.

Based on these directives, extensive activity is undertaken in defining organizational information security policy, structuring work programs for the implementation of supervision and information security mechanisms, establishing systems and integration of information security management, and planning and execution of information security controls, including the drafting of procedures.

In an era in which threat from external factors are increasing, Leumi is prepared for computer attacks and is taking steps to hedge the risks arising from various cyber attacks.

The operations and computer department of subsidiaries in Israel and abroad are based on independent systems, with the managements and boards of directors of those companies having professional and administrative responsibility. Within the context of a multi-year program, together with the overseas subsidiaries, the Bank is improving and upgrading the systems at the overseas subsidiaries to uniform computerized banking systems.

Hatam operates an array of computerized systems for the Arab Israel Bank (a subsidiary) and for the Union Bank. There is an agreement with them relating to computer services provided by Hatam, which includes operating services, computer systems development, consultancy services, organization and method services, back-ups, training and other services.

The main computer center of the Mortgage Division is located in Keshev, and it receives services from IBM, and the back-up site was set up in Tel Aviv.

The overseas subsidiaries are connected to each other and to the Bank in Israel via a private communication network. This system is used for voice communication as well as for transmitting encrypted data in a secured manner. The Bank invests in maintaining and developing Internet sites for the Bank's overseas subsidiaries based on the Bank's infrastructure. In addition, the technological infrastructure was upgraded to improve the availability of the systems.

Bank Leumi USA has outsourcing agreements with a number of U.S. companies regarding the information systems used for the management of its banking business.

In 2013, the Group invested in equipment including software some NIS 652 million, compared with some NIS 765 million in 2012. The budget was adapted to support the strategic goals as defined by the Bank Management, as well as the operating requirements for future banking. Projects carried out in 2013 were designed for the benefit of the customers, to increase their satisfaction, to reinforce their loyalty and to prevent their leaving.

The major investment in 2013 (as in previous years) focused on online areas and improving the "customer experience" through Leumi Digital, Leumi Cellular, trading on the capital market via the Internet,

In order to supply the needs of capital market customers, to strengthen the business connection with its customers and to withstand the competition in the market, some of the investments were directed, *inter alia*, to the development and expansion of data channels from the Bank to the systems of the customers in their offices.

In 2013, Project Calypso for replacing the WSS system in stages commenced. Further to the services developed in 2012 for Leumi Trade customers, in 2013, the services provided to these customers were expanded – including: the construction of an advanced interface for speedy trading in shares. ETFs, value-added services for Mega-Trade type active services, the addition of personalization, etc. In addition new Smart Bond models were added – advanced management of debenture portfolios and weekly Ma'of options in the derivatives market.

In 2012, after the Mabat Internet system was introduced including unique models for the advisor: shares, debentures, mutual funds, ETFs, daily bulletin, reviews, stock exchange notices, etc., this system was enhanced on a number of plains, most prominently being the combination of customer data in the system. The concentration of external and internal organizational information, in conjunction with customer data, to a uniform desktop turned Mabat into the most unique and advanced of all the advisor-support systems. Further upgrades in quantity and quality of incoming stock exchange data, and the improvement in design guarantees the maintenance of service at the highest level for the Bank's customers.

In the area of marketing websites, new developments have been added – integrating Google's search engine, assimilation of responsiveness in Leumi's website, the transfer of Facebook applications to the Bank's premises, Leumi Buzzer Youngster's Club – Students' Campaign and a new design.

In addition, the "Digital Assistant" service envelope on the Internet and cellular phones, were integrated, including a new and enhanced look of Leumi websites, and a range of new value customer offers. In addition, the services were expanded to reach retail and business customers.

In 2013, developments in the cellular phone continued and several new applications were developed: an application for information and trade by IPad and foreign securities, an appendix for approving a signature for transactions by the business customer by IPhone, Android and IPad, an application for information and execution of transactions by Android-based Tablet and a brand new service, the first in Israel, the possibility of depositing cheques by cellphone.

In 2013, a center for businesses for improving service and improving the customer experience for business customers was set up in Leumi Call.

The Bank's investments and expenses in respect of information technologies in 2013

Expenses recorded in the statement of profit and loss amounted to NIS 1,508 million (NIS 1,556 million in 2012), of which NIS 420 million (NIS 450 million in 2012) were recorded in salary and related, NIS 655 million (NIS 604 million in 2012) in depreciation expenses and NIS 433 million (NIS 502 million in 2012) in other expenses.

Costs in respect of the information technology setup which were not recorded in the statement of profit and loss, but recorded as assets in the financial statements in 2013, amounted to NIS 690 million, compared to NIS 738 million in 2012.

The balance of the assets in respect of the information technology setup as at 31 December 2013 amounted to NIS 2,095 million (NIS 2,167 million in 2012).

Against the background of various requirements by the authorities (Bank of Israel, Ministry of Finance etc.) for the execution of various directives, in 2013, the Bank incurred computer–related expenses estimated at some NIS 42 million (some NIS 44 million in 2012). In 2013, the Bank invested in the impaired debt system and in the risk management systems – combining risk management indices in the systems supporting the Bank's business activity.

The increase in investments in buildings and equipment is intended to adapt the logistical infrastructure and deployment of the Bank's branches to the expansion that has occurred in business activity, and to the operational needs of modern banking.

The Bank has been certified for quality standards from Israel Standards Institute in the following areas: software quality, data security, quality management systems, information technology services management, business continuity, safety and occupational hygiene, and fire safety.

This year, Leumi for the first time in 2012, contended with the category of large organizations and was awarded second place in the Yitzhak Rabin National Prize for Quality and Excellence. This competition is considered most prestigious in the area of quality and excellence in the State of Israel and its purpose is to raise the threshold of quality in Israel, to approve, streamline procedures and encourage various organizations and entities to be in a constant process of improvement.

The Israel Standards Institute awarded the Keshev facility in Leumi, for the first time, the prestigious Diamond Medal for 2012 which is given to companies with seven or more medals for quality. The Diamond Standard was also awarded in 2013.

See Note 7 to the financial statements for further details.

Intangible Assets

1. The Bank is the sole proprietor of the "Leumi" trademark, and its accompanying design logo, in the banking and finance services field in Israel.

2. In addition, the Group makes use of the names of its companies and their logos for the purposes of its activities, and the names of services and products, some of which are registered as trademarks and service marks.

3. The Group has registered databases in which information is stored, *inter alia*, regarding customers, suppliers and employees of Leumi, with advanced technological means that are designed to protect customer activity and the Bank's business activity, while reducing the risks arising from the use of information systems.

4. The Group holds various intellectual property rights and user rights in various computer programs and information systems for the purpose of managing its business, including the provision of services to customers.

5. The Group has intangible assets and goodwill from the acquisition of companies. For further information, see Note 6 to the financial statement, below.

Operating Segments, Activities in Products and Profit Centers in the Group

Operating Segments in the Group

This chapter describes the business development according to operating segments.

For a description of the methodology of the operating segments, see above in the chapter, "Description of Operating Segments".

The following are principal data according to operating segments of the principal balance sheet items as at 31 December:

Segments	Credit to the public			Deposits of the public			Total assets		
	2013	2012	Change	**2013**	2012	Change	**2013**	2012	Change
	NIS millions		%	NIS millions		%	NIS millions		**%**
Households(1)	**100,243**	90,492	10.8	**118,634**	128,194	(7.5)	**100,913**	91,216	10.6
Small businesses	**23,299**	21,733	7.2	**22,830**	19,666	16.1	**23,326**	21,757	7.2
Corporate banking	**60,646**	70,252	(13.7)	**22,816**	26,281	(13.2)	**62,482**	71,905	(13.1)
Commercial banking	**49,630**	49,908	(0.6)	**51,878**	50,108	3.5	**53,931**	50,758	6.3
Private banking	**6,455**	8,170	(21.0)	**34,794**	38,338	(9.2)	**11,527**	13,167	(12.5)
Financial management capital markets and others	**601**	709	(15.2)	**35,051**	26,951	30.1	**122,181**	127,357	(4.1)
Total	**240,874**	241,264	(0.2)	**286,003**	289,538	(1.2)	**374,360**	376,160	(0.5)

(1) Credit to households also including housing loans (mortgages) increased by 10.8% and, after canceling housing loans, increased by 11.2%. Housing loans amounted to NIS 68.5 billion at the end of 2013, having increased by 10.6%.

.

Following are principal data according to operating segments of off-balance sheet items and data on customers' balances in the capital market:

Segments	Guarantees and documentary credit			Securities portfolios, including mutual funds		
	2013	2012	Change	**2013**	2012	Change
	NIS millions		%	NIS millions		%
Households	**396**	443	(10.6)	**107,194**	94,329	13.6
Small businesses	**1,456**	1,564	(6.9)	**10,885**	6,764	60.9
Corporate banking	**28,038**	27,652	1.4	**62,850**	59,996	4.8
Commercial banking	**6,574**	6,470	1.6	**56,885**	48,660	16.9
Private banking	**399**	387	3.1	**85,442**	85,065	0.4
Financial management – capital markets and others	**774**	821	(5.7)	**280,839**	232,768	20.7
Total	**37,637**	37,337	0.8	**604,095**	527,582	14.5

Return on equity by operating segments

The equity for the purpose of calculating the capital to risk assets ratio (Tier 1 and Tier 2 capital) was allocated to the segments according to the relative share of each segment in the total of all the weighted risk assets of the Group, and according to the allocation of Pillar 2 equity for each segment according to its characteristics and constituents.

The profit of the operating segments has been adjusted for risk capital in each segment. The risk-adjusted yield has been calculated as the ratio of the adjusted profit to shareholders' equity allocated to the segment, constituting the share of the allocated risk capital (Tiers 1 and 2).

The following table shows the breakdown of net profit by operating segment:

Segment	**2013**	2012	Change
	NIS millions		%
Households	**109**	447	(75.6)
Small businesses	**288**	319	(9.7)
Corporate banking	**965**	392	146.2
Commercial banking	**412**	434	(5.1)
Private banking	**(15)**	77	-
Financial management	**228**	(613)	+
Other	**(40)**	(125)	+
Total	**1,947**	931	109.1

Below is the return on risk adjusted capital (RORAC) and the economic value added (EVA) taking into account the cost of capital according to the multi-year return set out in the work plan, by operating segments:

The RORAC amounts were calculated according to the allocation of all of the Bank's capital between the segments (according to actual capital adequacy pursuant to Basel II).

Segment	**As at 31 December 2013**	**As at 31 December 2012**
	Allocation of all the capital	Allocation of all the capital
	RORAC	RORAC
	%	%
Households	**1.9**	9.6
Small businesses	**17.2**	21.1
Corporate banking	**11.8**	4.3
Commercial banking	**9.0**	10.3
Private banking	**(1.6)**	8.3
Financial management – capital market	**5.6**	(18.3)
Other	**(8.1)**	(29.9)
Total to net profit	**7.6**	3.8

For further details regarding activities of the principal investee companies, see below the chapter, "Investments in Investee Companies".
A breakdown of the results of the operating segments is presented in note 27 to the financial statements.

1. Household Segment

General

Banking in the household segment provides a range of financial services and products to individual customers according to their varying needs, while segmenting customers according to demographics, place of residence, occupation, financial characteristics and stages of life, from which the customers' financial needs are deduced.

Objectives and strategy

The following information is "forward-looking information." For the meaning of this term, see above in the chapter, "Description of the Banking Corporation and Forward-Looking Information"

The strategic objectives for banking in the household segment are to broaden the customer base and expand the activities of existing customers, while placing emphasis on the provision of efficient service that is adapted to their needs, and consequently, an expansion of activity and an increase in profitability of the household segment. Household credit is an important growth driver for retail activity, in light of the high level of dispersion and good risk management capabilities.

Project "Advancing Together"

In 2011, the Bank commenced the "Advancing Together" project which is aimed at upgrading the customer experience, while improving operating efficiency. As part of this project, several activities and procedures that are not involved with contact with customers were taken from the branches and transferred to the remit of national centers of expertise. At the same time, in the branch and various channels, new initiatives were launched to improve customer experience and service and adapt them to customer's needs. The project was implemented gradually in all of the Bank's branches and full deployment was achieved at the end of 2013.

In addition, two credit centers dealing with requests for credit from the branches were set up.

Further to the Advancing Together" process, with effect from 2014 and thereafter, the Bank will focus on the subject of customer experience. The strategic focus on this subject is based on technological infrastructure and customer experience-supporting processes.

The important points of emphasis in the household segment are:

- A systematic and constant focus on improving the **level of service** to the customer by upgrading employees' skills, and measuring and controlling the work procedures and customer interface. Improving customer service will increase customer satisfaction and loyalty, through creating advantages among the groups of customers by providing differential value proposals.
- **Broadening the availability of service to customers** by increasing the number of branches and adapting them to future banking needs, while integrating advanced automated instruments, and adapting them to the various customers’ needs.
- **Expanding the direct marketing channels**: advanced telephone, cell phone and Internet response services and instruments for self-service performance of financial operations;
- **Developing financial products and services** by providing professional and objective counseling in relation to financial investment products and pension products that correspond to the needs of customers, while using data mining and analytical models to analyze and forecast the customers’ financial activities and needs.
- Systematic, information-based **initiative** *vis-à-vis* customers in all operating segments: investments, pension counseling, consumer and commercial credit and current account services.
- **Collaboration with companies in the Group,** in order to utilize the Group’s abilities in providing comprehensive banking solutions to customers.

Structure of the segment

Household banking segments its customers according to their characteristics, needs, preferences and scope of activity, and develops services, products and distribution channels for them according to this segmentation. Service to these customers is in a range of channels and is provided both through a wide spread of 241 branches (including 16 counters and 36 branches of the Arab Israel Bank Ltd.) located throughout the country and organized into eight districts on a geographical basis, and through the Leumi Call center, the Internet, Leumi information terminals, cellular, and through advanced Internet solutions adapted to meet customers' needs.

Service to customers in branches is provided by banking teams divided into customer segments. All aspects of customer service are coordinated by these teams, who specialize in providing service according to the customer’s characteristics and needs.

Legislative Restrictions, Regulations and Special Constraints that apply to Banking in the Household Segment

The Bank, and the household segment, in particular, operates within the context of laws, regulations and directives of authorities imposed on the banks by the Banking Supervision Department, the Israel Securities Authority, the Commissioner of the Capital Market, Insurance and Savings, and by the Antitrust Commissioner.

Changes in the Markets of the Household Segment or in Customer Characteristics –

The household segment was affected by changes in the demographic and economic data for the population of the State, by changes in private consumption and by customers' saving characteristics. Private consumer expenditure increased in real terms in 2013 by 4.0%, and in terms of private consumption per capita, by 2%. These data indicate a slightly faster expansion that 2012, in which expenditure for private consumption in real terms increased by some 3.2%. This is mainly explained by an increase in the consumption of durable products in 2013, compared with a decline in 2012, mainly due to an increase in the purchase of motor vehicles for private use.

The segment is taking steps, *inter alia*, to expand the number of its customers receiving telephone service provided by the Leumi Call center, to which hundreds of thousands of customers are currently connected, and who perform most of their day-to-day transactions in their accounts via the center.

Each day, thousands of operations are performed via the Internet. In 2013, the Bank continued making technological improvements and adaptations of Leumi's websites to the various customer segments. In addition, developments in technology enable the Bank to develop products and services according to customer requirements.

Critical success factors in the segment:

- Maintaining pro-active service pursuant to the needs and wishes of the customers;
- Efficiency: constant examination of retail operating costs against the benefits derived from them, and reduction of the cross subsidization between the various activities and populations.
- Broadening the exposure and availability of direct technological channels (Internet and telephone) to customers and broadening the geographical distribution (ATMs).
- Quality: abiding by the rules of consistent and methodical documentation, while strictly adhering to rules of compliance with consumer laws and regulations.
- Distribution and availability of points of sale and service: adapting the distribution of the branches and adapting operating hours to the region and type of population;
- Provision of investment counseling and pension counseling services by making available suitable manpower and technological support.

Main entry and exit barriers in the segment

- The technological and physical infrastructure (branch distribution) and the quality of the manpower are relative advantages of banking in the household segment, and constitute entry barriers to competitors. The importance of the infrastructure increases as the regulatory requirements increase.
- The investment required in physical and technological infrastructure constitutes a barrier to both entry and exit.
- The development of analytical capabilities to effectively adapt solutions for customers based on historical data on customer activity and market behavior.
- The training of skilled human resources in light of increasingly strict and frequently changing regulations.

Alternatives to banking products and services in the segment

The banks constitute the main entity providing objective counseling to customers – both in the capital market and in the pension field.

Current accounts can only be managed at banks. Other products and services may be purchased outside of the banks as well, as follows:

Consumer credit – credit card companies, retail food chains, insurance companies

Capital market – brokers, insurance companies, fund managers

Pension savings – pension marketers (insurance companies, companies managing provident funds, supplementary training funds, pension funds and insurance agents, private pension consultants)

Mortgages - contractors, construction companies, insurance companies.

Structure of the competition

The fundamental principles of success are: the segmentation and understanding the requirements of customers and the provision of value proposals for contending with the competition, the availability and correct usage of distribution channels, while improving efficiency.

Competition in retail banking has been developing in recent years from financial and other entities, primarily from credit card companies – while in the field of consumer credit, competition is developing from mortgage banks, insurance companies and retail marketing chains. The competition is created by entities that are not subject to the supervision of the Bank of Israel, or not supervised at all, and do not operate under the restrictions that apply to the banks.

Directives issued by the Supervisor of Banks, which make it easier for customers to move from bank to bank, affect competition between banks in this segment.

In the field of pension counseling, the competition over customers is intense; competitors include insurance agents, pension arrangement managers and companies that manage their own pension funds.

Products and services of the segment

As part of its overall service concept, the Bank invests considerable resources in development and the creation of a high level of availability of a range of channels: telephone, the internet and branches, in order to provide customers with an interface with the Bank for executing transactions and receiving information.

In the private credit field, the Bank offers customers, various credit products which are appropriate to their needs and the various stages in their lives, *inter alia*, it is possible to receive pre-approved loan, limited in amount, via all of the self-service channels, including ATMs, according to the characteristics and needs of each customer.

In the investments field, the Bank offers a variety of both single deposit and installment-based deposits, and savings schemes, with various linkage bases, for periods that suit the customer, as well as a variety of investment products, including structured deposits in Israeli and foreign currency and savings schemes. The Bank also offers investment counseling and pension counseling services.

Pension Counseling

The balances of the pension assets held by customers receiving consultation in the Leumi Group known at the end of December 2013, including advance training funds in respect of which consultancy is provided in the framework of pension consulting and/or investment consulting amounts to some NIS 18.5 billion.

Customers

The Bank is able to offer its services with adaptations to the following various population groups in the segment: households with medium to low levels of wealth and current account requirements, customers with growth, for example,: young people, discharged soldiers, students and new immigrants, pensioners, salary-earners, mortgage customers and wealthy private customers.

For further details, see above in the chapter, "Description of Operating segments".

Marketing and Distribution

The following information is "forward-looking information." For the meaning of this term, see above in the chapter, "Description of the Banking Corporation and Forward-Looking Information".

Household banking is based on a countrywide distribution network, professional and skilled manpower and technological systems that enable the provision of efficient service to customers, as well as measurement and control tools for the Management. The Bank sees strategic importance in a correct deployment of branches. In addition, emphasis is placed on offering service via a multitude of channels, while maintaining a uniform customer experience and level of service. The principal distribution channel of the household segment is the branch channel, while some of the direct channels - the Internet, Leumi Call and ATMs - are in a continuing growth trend, both for execution of transactions and for informational needs. The Bank also makes use of direct mailings, advertising on websites in general and on the Bank's websites in particular, and other media, including newspapers and television. In addition, Leumi operates a number of communication channels on social networking media including a Twitter account and banking blog and an exclusive page on Facebook. Through these channels, the Bank provides a service to customers, and general and marketing information for the use of the public.

Marketing activity is based on advanced analytical information systems, enabling customers' needs and behavior to be characterized, with a view to offering customers products and services tailored to their needs.

Human Capital

In 2013, the average number of positions assigned to the household segment totaled 7,007, of which 1,450 were management staff, compared with 7,169 positions in 2012, of which 1,472 were management staff.

Tenured employees, who have been trained for various positions according to banking needs, are employed in the branches. In addition, external staff are employed in basic positions, having received appropriate training.

Credit Cards

See below in "Activity in Products" in this chapter.

Housing Loans – Mortgages -– These loans are provided by the Bank through the Leumi Mortgage Department in 102 representative offices operating Leumi branches and seven independent representative offices.

The Leumi Mortgage Department develops tools which are intended to help customers plan the appropriate mortgage for them now and in the future. Within this framework, the Leumi Mortgage Department off those interested in a mortgage a comprehensive Internet website, a guide including an explanatory video clip and a Smartphone application supporting customers in mortgage planning. The Bank also offers its customers the "pooling method" which adapts the mix of loan paths to the customer's needs.

The Bank's policy is to continue focusing its activity in the loan segment for residential apartment purchases and in the loan segment using residential apartments as collateral.

In addition, the Bank also provides loans for purchasing groups; see Exhibit E – Economic Sectors.

The following table presents data on the performance of new loans provided and loans refinanced for the purchase of residential apartments, and of collateralization of residential apartments in the household segment:

	2013	2012	
	Annual total	Annual total	Change
	NIS millions		%
From bank funds	**14,699**	13,665	7.6
From Ministry of Finance funds:			
Directed loans	**38**	34	11.8
Bullet loans	**28**	15	86.7
Total new loans	**14,675**	13,714	7.7
Refinanced loans	**3,083**	1,597	93.0
Total performance	**17,848**	15,311	16.6

Data relating to the risk characteristics of housing loans

Disclosure of housing loans

The following are data relating to the risk characteristics of housing loans pursuant a letter of the Bank of Israel dated 15 May 2011, developments in credit risk and how they are managed, including consideration of steps taken by the Bank to contend with these risk characteristics.

The definitions mentioned in the disclosure below (for example, repayment ratio, rate of financing, etc.) are in accordance with the definitions of the Bank of Israel.

Development of credit balance for housing, net:

	Balance of credit portfolio	Rate of growth
	NIS millions	%
December 2011	54,386	
December 2012	60,294	10.9
December 2013 *	**68,152**	**13.0**

* With effect from 2013, data for housing credit include housing credit granted in Leumi other than through the mortgage department.

In recent years, there has been an increase in the volume of housing credit, arising from, inter alia, an increase in the demand for housing units and a rise in the prices of housing units. Most of this credit constitutes credit for the purpose of acquiring residential apartments.

Development of credit balance, net by linkage basis:

	Unlinked	Percentage of credit portfolio	Index-linked	Percentage of credit portfolio	Foreign currency	Percentage of credit portfolio	Total portfolio
	NIS millions	%	NIS millions	%	NIS millions	%	NIS millions
December 2011	22,973	42.2	29,802	54.8	1,611	3.0	54,386
December 2012	26,234	43.5	32,522	53.9	1,538	2.6	60,294
December 2013 *	**31,740**	**46.6**	**34,718**	**50.9**	**1,694**	**2.5**	**68,152**

* With effect from 2013, data for housing credit include housing credit granted in Leumi other than through the mortgage department.

Development of balance of housing credit portfolio, at variable and fixed interest:

	Fixed		Variable			Total credit portfolio
	Unlinked	Index-linked	Unlinked	Index-linked	Foreign currency	
	NIS millions					
December 2011	1,142	11,125	21,831	18,677	1,611	54,386
December 2012	2,144	10,698	24,090	21,824	1,538	60,294
December 2013 *	**4,289**	**10,583**	**27,451**	**24,135**	**1,694**	**68,152**

* With effect from 2013, data for housing credit include housing credit granted in Leumi other than through the mortgage department.

Development of new housing credit balance by interest path:

The development of new credit according to variable and fixed interest paths (a variable interest loan is a loan where the interest that it bears is likely to change over the life of the loan) is as follows:

	2013 *				**2012**	2011
	Fourth quarter	Third quarter	Second quarter	First quarter	Annual average	Annual average
	Percentage of loans granted %					
Fixed – linked	**19.9**	10.5	13.3	10.9	13.3	10.0
Variable – linked to index – every 5 years and over	**21.8**	28.9	31.1	31.3	40.4	26.7
Variable – linked up to 5 years	**2.6**	2.2	2.2	2.5	4.5	13.1
Fixed – unlinked	**17.1**	14.4	13.6	14.3	8.4	3.8
Variable – unlinked– 5 years and over	**9.0**	11.5	9.0	9.3	4.5	-
Variable – unlinked up to 5 years	**28.4**	30.8	28.9	29.1	27.5	42.0
Variable – foreign currency	**1.2**	1.7	1.9	2.6	1.4	4.4

* With effect from 2013, data for housing credit include housing credit granted in Leumi other than through the mortgage department.

The percentage of new credit extended by the Bank in variable interest housing loans during 2013 stood at 72%, compared with 79% in 2012. The figures relate to all of the various interest paths and linkage segments, including loans in which the interest varies each period of five years and more. After canceling the effect of loans in which the rate of interest is variable, which varies each period of five years and more, which the directive of the Banking Supervision Department of 3 May 2011 departs from the definition of variable interest loans, the percentage of housing credit at variable interest which stood at 33.3% during 2013, similar to the average for the whole of 2012.

The balance of the past due portfolio in housing loans more than 90 days in arrears is as follows:

	Balance of recorded debt	Amount in arrears	Percentage of amount in arrears
	NIS millions		%
December 2011	54,888	918	1.7
December 2012	60,738	829	1.4
December 2013 *	**68,627**	**810**	**1.2**

* With effect from 2013, data for housing credit include housing credit granted in Leumi other than through the mortgage department.

The allowance for credit losses as at 31 December 2013, including the collective allowance on housing loans (hereinafter: "the overall allowance") as required in a letter of the Bank of Israel dated 1 May 2011, is NIS 475 million, representing 0.69% of the housing credit balance, compared to the balance of the allowance as at 31 December 2012, amounting to NIS 444 million, representing 0.73% of the housing credit balance. The increase in the allowance for credit losses derives from an adjustment of the collateral allowance for housing loans as required in the Bank of Israel directives of 21 March 2013 amounting to NIS 50 million.

Data relating to new housing credit:

In 2013, the Bank extended new housing loans amounting to NIS 14.8 billion of the Bank's funds.

Development of the rate of financing*, in new credit, above 60%:

The development of new credit extended by Leumi Mortgage Bank at a rate of financing higher than 60% is as follows: (The rate of financing is the ratio between the rate of credit approved for a borrower (even if all or part thereof has not yet been actually extended) and the value of the asset mortgaged, at the time of extending the credit facility.)

	2013					2012				2011
	Fourth quarter	Third quarter	Second quarter	First quarter	Annual average	Fourth quarter	Third quarter	Second quarter	First quarter	Annual average
Rate of financing	%									
Between 60% and 70%	17.0	16.5	19.2	20.9	22.6	20.6	22.6	23.2	24.5	23.0
Between 70% and 80%	15.4	16.7	16.9	16.0	12.9	12.9	13.6	12.0	12.8	12.5
Above 80%	0.7	0.8	0.9	1.3	3.5	3.5	4.0	3.5	2.5	3.2

Development of the rate of financing*, balance of credit portfolio:

The average rate of financing of the credit portfolio balance at 31 December 2013 was 49.5%, compared to 50.6% in 2012.

Development of new credit, in which the repayment ratio is lower than 2:

Loans made in 2013 in which the repayment ratio is lower that 2 to income-earners of NIS 10,000 and below, at the date of approval of the credit, stood at 0.9% of the total extensions of new credit, slightly than the average in 2012 and compared with an average of 2% for 2010 - 2012 (the repayment ratio is calculated by dividing the fixed monthly income of the borrower by the total monthly repayments in respect of the existing mortgage loans and in respect of the new loan).
This calculation complies with the Bank of Israel directives for the purposes of reporting pursuant to Proper Conduct of Banking Business Management Regulation no. 876.

Development of new credit, in which the repayment dates are longer than 25 years:

The percentage of the new credit of housing loans in 2013, in which repayment dates according to loan contracts longer than 25 years, stood on average at 30% of the total of new credit extended, compared 31% in 2012 and 31% in 2011.

In general, the Bank does not extend new loans whose terms enable the borrower to make a payment which is lower than the interest accrued on the loan, except in extraordinary cases.

The Bank does not extend loans secured by a secondary mortgage, except in extraordinary cases.

According to the Bank's credit policy, the Bank extends new loans in which the information the Bank has on the borrower or on the collateral, at the time of granting the loan, is complete, updated and verified.

Developments in credit risks

In recent years, against a background of rising demand for housing units, both for residential purposes and for investment, there has been a significant increase in housing prices, resulting in a substantial increase in the level of housing credit. Against the backdrop of this price increase, the risk inherent in the provision of loans at high financing rates has increased, attributable to the high debt burden on the borrower and a higher exposure when there is an impairment in the security.

In addition, the low interest rates which prevailed in the economy in recent years, particularly unlinked Prime interest, led to a sharp increase in the proportion of unlinked variable interest loans, out of the total credit to the public in the mortgage market. Accordingly, in an environment of an increase in interest rates, the borrowers are exposed to an increase in the level of mortgage payments.

As a result of the economic developments that have occurred in recent years, as presented above, the Bank adopted a number of measures in order to contend with the increase in the abovementioned credit risks.

- As part of the risk management, it was decided to tighten the administrative limits for the following features: high financing rates, current monthly repayment ability, credit rating according to the Bank's internal statistical model, loan products/paths, interest types and extent of loan.

- As part of credit risk management, the Bank periodically performs stress scenarios that have examined the effect of a possible fall in the value of securities, an increase in interest rates and the effect of other macroeconomic variables on the Bank's results.

As a part of its capital planning and its goals, the Bank has maintained further "capital buffers" to deal with higher risk features, such as: a capital buffer in respect of loans at high financing rates, a capital buffer in respect of the gap between the current rate of allowance for credit losses and the average rate over an economic cycle and a capital buffer in respect of the possibility of a fall in real estate prices.

The average loan extended by the Bank in 2013 was NIS 551 thousand, compared with NIS 530 thousand in 2012, NIS 540 thousand in 2011 and NIS 665 thousand in 2010.

The quality of the housing credit portfolio is good, this, relying on the data for extent of debts in arrears, the credit loss allowances and the problem debts as a percentage of the Bank's total credit portfolio, as well as the low rate of losses on the liquidation of assets.

Update of directives on the subject of residential real estate

On 19 February 2013, the Supervisor of Banks published a draft update of the directives regarding residential property. On 21 March 2013, the directives were updated and the circular was published.

The directives provide, *inter alia*, that commencing the financial statements for the second quarter of 2013, the ratio of the collective allowance to the balance of the housing loans will stand at a minimum rate of 0.35%. This does not apply to housing loans in respect of which an allowance according to the extent of arrears or an individual allowance is held. In the financial statements for the first quarter of 2013, an allowance of NIS 50 million was made as a result of this directive.

Below is a summary of the results of operations of the Household Segment:

	Banking and finance	Credit cards	Capital market	Mortgages	Overseas activity: Banking and finance	Overseas activity: Mortgages	Total
	2013						
	NIS millions						
Net interest income:							
From external sources	33	240	6	2,662	(11)	11	2,941
Intersegmental	1,735	(34)	(3)	(2,008)	18	(1)	(293)
Non-interest income:							
From external sources	572	513	434	115	6	-	1,640
Intersegmental	-	166	-	-	-	-	166
Total income	2,340	885	437	769	13	10	4,454
Expenses in respect of credit losses	117	13	-	48	1	-	179
Operating and other expenses:							
To external sources	2,768	673	381	251	14	6	4,093
Intersegmental	7	(6)	-	-	-	-	1
Profit (loss) before taxes	(552)	205	56	470	(2)	4	181
Provision for (benefit from) taxes on profit	(201)	60	21	168	1	-	49
Profit (loss) after taxes	(351)	145	35	302	(3)	4	132
Group share in profits of companies included on equity basis after tax	-	4	-	-	-	-	4
Net profit attributable to non-controlling interests	-	(27)	-	-	-	-	(27)
Net profit (loss)	(351)	122	35	302	(3)	4	109
Return on equity							1.9%
Average balance of assets	21,407	9,025	149	65,191	55	206	96,033
Of which: investments in companies included on equity basis	-	2	-	-	-	-	2
Average balance of credit to the public	21,089	8,815	149	65,039	54	206	95,352
Average balance of liabilities	121,803	1,042	-	272	918	8	124,043
Average balance of deposits of the public	121,613	42	-	-	918	8	122,581
Average balance of risk assets	23,703	8,762	144	35,323	273	72	68,277
Average balance of mutual funds and supplementary training funds	-	-	65,642	-	-	-	65,642
Average balance of securities	-	-	47,996	-	176	-	48,172
Average balance of other assets under management	4,357	-	-	-	-	-	4,357
Margin from credit-granting activities*	995	205	3	654	(8)	10	1,859
Margin from deposit-taking activities*	773	1	-	-	15	-	789
Total net interest income	1,768	206	3	654	7	10	2,648
Balance of credit to the public	22,112	9,358	167	68,345	50	211	100,243
Balance of deposits of the public	117,675	40	-	-	912	7	118,634

* The margin is, in effect, the interest gap between the interest received from the granting of credit and the interest paid on raising deposits, and the transfer prices set by the Finance Division.
This comment relates to all of the operating segments.

Household Segment (cont.):

	Banking and finance	Credit cards	Capital market	Mortgages	Overseas activity: Banking and finance	Overseas activity: Mortgages	Total
	2012						
	NIS millions						
Net interest income:							
From external sources	(605)	251	8	2,230	(11)	11	1,884
Intersegmental	2,576	(50)	(5)	(1,623)	18	(1)	915
Non-interest income:							
From external sources	582	496	456	82	6	-	1,622
Intersegmental	5	177	-	48	-	-	230
Total income	2,558	874	459	737	13	10	4,651
Expenses in respect of credit losses	62	18	-	(11)	2	-	71
Operating and other expenses:							
To external sources	2,629	636	314	256	14	6	3,855
Intersegmental	-	(5)	-	22	-	-	17
Profit (loss) before taxes	(133)	225	145	470	(3)	4	708
Provision for (benefit from) taxes on profit	(50)	69	52	165	-	-	236
Profit (loss) after taxes	(83)	156	93	305	(3)	4	472
Group share in profits of companies included on equity basis after tax	-	2	-	-	-	-	2
Net profit attributable to non-controlling interests	-	(27)	-	-	-	-	(27)
Net profit (loss)	(83)	131	93	305	(3)	4	447
Return on equity							9.6%
Average balance of assets	19,798	8,216	130	58,915	67	191	87,317
Of which: investments in companies included on equity basis	-	2	-	-	-	-	2
Average balance of credit to the public	19,454	8,007	130	58,709	67	191	86,558
Average balance of liabilities	126,515	1,020	-	5,391	879	9	133,814
Average balance of deposits of the public	126,297	37	-	3,411	879	9	130,633
Average balance of risk assets	21,503	8,036	128	32,147	224	67	62,105
Average balance of mutual funds and supplementary training funds	-	-	53,968	-	-	-	53,968
Average balance of securities	-	-	48,990	-	175	-	49,165
Average balance of other assets under management	204	-	-	4,930	-	-	5,134
Margin from credit-granting activities*	912	200	3	608	(7)	10	1,726
Margin from deposit-taking activities*	1,059	1	-	(1)	14	-	1,073
Total net interest income	1,971	201	3	607	7	10	2,799
Balance of credit to the public at 31 December 2012	19,907	8,387	138	61,794	62	204	90,492
Balance of deposits of the public at 31 December 2012	127,229	32	-	-	924	9	128,194

Main Changes in the Volume of Activity

Total credit to households at the end of 2013 amounted to NIS 100.2 billion, an increase of 10.8%. Of this, consumer credit totaled NIS 31.7 billion, an increase of 11.2% and credit for housing totaled NIS 68.5 billion, an increase of 10.6%. Deposits of the public fell from NIS 128.2 billion to NIS 118.6 billion, a decrease of 7.5%.

Main Changes in the Net Profit

Net profit from the household segment totaled NIS 109 million in 2013, compared with NIS 447 million in the corresponding period in 2012, a decrease of NIS 338 million, 75.6%.

The main reasons for the increase in profits are as follows:
A decrease in interest income amounting to NIS 151 million, an increase in operating expenses of NIS 222 million, and an increase in expenses in respect of credit losses amounting to NIS 108 million, deriving, *inter alia*, from the adjustment of the collective allowance for housing loans as required by Bank of Israel regulations.

Mortgages

The net profit in mortgages amounted in 2013 to NIS 306 million, compared with NIS 309 million in 2012, a decrease of NIS 3 million. Total income increased by NIS 32 million from NIS 747 million in 2012 to NIS 779 million in 2013 and operating expenses fell by NIS 27 million. On the other hand, there was increase in credit loss expenses amounting to NIS 59 million, mainly deriving from the adjustment of the collective allowance for housing loans as required by a directive of the Bank of Israel.

2. Small Business Segment

General

Banking in the small business segment provides a variety of financial services and products to small and medium-sized business customers according to their varying needs, while segmenting customers according to their business activity turnovers, the extent of their credit needs and the sector in which their businesses operate.

The Bank also handles the personal accounts of the proprietors of the businesses in the segment, such that they receive all their services in one place.

Objectives and Strategy

The following information is "forward-looking" information. For the meaning of this term, see above in the chapter, "Description of the Banking Corporation and Forward-Looking Information".

The strategic objectives of banking in the small business segment are to increase market share and profitability by broadening the customer base and expanding the activities of the existing customers, while placing emphasis on the provision of efficient service and a customer experience tailored to their needs.

In connection with the project "Advancing Together", see above in Household Segment, in this chapter.

The business line emphases in the small business segment are:

- Systematic and constant focus on improving **the level of service** to the customer by upgrading employees' skills, and measuring and controlling the work procedures and customer interface.
- **Expanding the direct marketing channels**: advanced telephone, fax, e-mail mobile and Internet response services.
- Developing financial products and services tailored to the needs of customers, using data and analytical models to analyze and forecast the customers' financial activities and needs.
- Systematic, information-based **initiative** *vis-à-vis* customers in all products: commercial credit, consumer credit, international trade, investments and current account services; improving the level of service in order to increase customer satisfaction and loyalty, by creating advantages for groups of customers through differential service**.**
- **Collaboration with companies in the Group,** in order to exploit the Group's abilities in providing comprehensive banking solutions to customers.
- Increasing the use of analytical models as supporting tools for decisions regarding client activities.

Structure of the Segment

The small business segment provides a variety of services to small and medium-sized business customers. These customers receive services from business teams in the branches, who specialize in the needs of the segment, and from an Internet channel designated for the segment's customers.

The segment specializes in the provision of banking solutions, including counseling with regard to commercial credit, investments and routine business activities, while determining sub-segments by level of activity and risk.

The main products supplied to the small business segment are credit and investment products, unique financial products and credit cards.

Legislative restrictions, regulations and special constraints that apply to the Segment:

The small business segment in particular operates within the context of laws, regulations and directives issued by the authorities, imposed on the banks by the Banking Supervision Department, the Israel Securities Authority, the Commissioner of the Capital Market, Insurance and Savings and by the Antitrust Commissioner.

Developments in the markets of the segment, or changes in the characteristics of its customers:

There were no significant changes in the small business segment during the past year.

Critical success factors in banking for small businesses:

Critical success factors in the segment are:

- High levels of management and interpersonal capabilities of the bodies responsible in the business centers.
- Familiarity with the customers, including their financial position, and the prospects/risks inherent in working with them;
- Ongoing monitoring of the changes occurring in the market in order to identify potential and to avoid risk; credit risk management and control;
- Quality: abiding by the rules of consistent and methodical documentation, and strictly abiding by rules of compliance with consumer laws and regulations;
- The distribution and availability of points of sale and service: expanding the distribution of the branches and adapting operating hours to the region and types of businesses;
- Increasing the exposure and availability of direct channels to customers;
- Focusing on the provision of proactive service and initiatives according to the needs and wishes of the customers.

Main entry and exit barriers in the segment

- The technological and physical infrastructure (branch distribution) and the quality of the manpower are relative advantages of banking in the small business segment, and constitute entry barriers to competitors. The importance of the infrastructure increases as the regulatory requirements increase.
- The investment required in physical and technological infrastructure constitutes a barrier to both entry and exit.
- The training of high-quality human resources possessing a high level of skill and familiarity with the customers' fields of activity.
- The development of analytical capabilities to effectively adapt solutions for customers based on historical data on customer activity and market behavior.

Alternatives to the products and services

In recent years, the competition in the small business segment has become increasingly intense. The direct competitors are all commercial banks in Israel and insurance companies.

Business Credit – insurance companies, credit card companies, suppliers

Capital Market – brokers, insurance companies, fund managers

Competition

The competition that the Bank has been facing in the small to medium-sized business segment has been intensifying in recent years. The competitors that the Bank faces include all commercial banks in Israel, and recently, also credit card companies and insurance companies.

The Bank competes by exploiting its expansive distribution advantages, professional and skilled manpower in the various banking fields and its data processing ability, all of which enable Leumi to be proactive and offer customers high-quality products and services.

Structure of the Competition

The main competition is between the major banks. In recent years, the smaller banks have been expanding their activities in this segment by means of aggressive marketing tactics and the use of price strategy.

In addition, competition has been developing recently from financial and other entities, primarily from credit card companies by means of supplier cards, and from insurance companies, which are showing an interest in financing small businesses.

Directives issued by the Supervisor of Banks, which make it easier for customers to move from bank to bank, are expected to increase the competition between banks in this segment.

Segment Products and Services

The services provided include, *inter alia*, ongoing financing according to customers’ needs, financing of investments to maintain and expand activity, the provision of solutions in the field of financing and international trade. In addition, the service includes banking services for companies' employees and management.

In the investments field, Leumi offers a variety of both single deposit and installment-based deposits, and savings schemes, with various linkage bases, for periods that suit the customer, as well as a variety of investment products, including structured deposits in Israeli and foreign currency, savings schemes, provident funds and mutual funds.

In addition, Leumi has invested considerable resources in development and has reached a high level of multi-channel availability (telephone, fax, e-mail, mobile and the internet), in order to provide customers with an efficient interface with the Bank for executing transactions and receiving information any place and any time.

Customers

The customers associated with this segment are characterized by diverse business activities (small to medium sized) and a great number and variety of sectors and fields. For further details, see above, in the chapter, "Description of Operating segments".

Marketing and Distribution

The small business segment is based on a nationwide distribution network, professional and skilled manpower, technological systems that enable the provision of efficient service to customers, as well as measurement and control tools for Management. Leumi sees strategic importance in a broad distribution network; consequently, teams are established in most of the branches in the Banking Division for handling customers in the segment, with the emphasis on deepening the familiarity with these customers and their needs, and on finding appropriate solutions for them. Marketing activity is based on advanced information systems that enable activities to be initiated with existing customers and with potential customers.

Human Capital

In 2013, the average number of positions assigned to the small business segment totaled 1,922 of which 476 were management staff, compared with 1,847 positions, of which, 483 were management staff, last year.

The employees engaged in this segment are mainly employees with academic education. In addition, employees receive regular professional training in various fields of banking.

Below is a summary of the results of operations of the Small Business Segment:

	Banking and finance	Credit cards	Capital market	Mortgages	Real estate	Overseas activity Banking and finance	Overseas activity Real estate	Total
	2013							
	NIS millions							
Net interest income:								
From external sources	752	22	1	3	289	47	11	1,125
Intersegmental	(87)	(3)	-	(2)	(65)	(14)	(5)	(176)
Non-interest income:								
From external sources	350	117	26	-	78	15	2	588
Intersegmental	2	(44)	-	-	-	-	-	(42)
Total income	1,017	92	27	1	302	48	8	1,495
Expenses in respect of credit losses	78	(1)	-	-	21	13	1	112
Operating and other expenses:								
To external sources	683	57	16	-	132	33	4	925
Intersegmental	2	4	-	-	-	-	-	6
Profit before taxes	254	32	11	1	149	2	3	452
Provision for taxes on profit	91	10	4	-	54	-	1	160
Profit after taxes	163	22	7	1	95	2	2	292
Net profit attributable to non-controlling interests	-	(4)	-	-	-	-	-	(4)
Net profit	163	18	7	1	95	2	2	288
Return on equity								17.2%
Average balance of assets	13,966	907	23	90	6,474	877	262	22,599
Average balance of credit to the public	13,956	893	23	90	6,473	877	262	22,575
Average balance of liabilities	16,584	1,526	-	-	3,888	612	94	22,704
Average balance of deposits of the public	16,551	-	-	-	3,784	612	94	21,041
Average balance of risk assets	11,430	731	21	56	6,409	989	262	19,898
Average balance of mutual funds and supplementary training funds	-	-	3,081	-	-	-	-	3,081
Average balance of securities	-	-	6,411	-	-	9	-	6,420
under management	210	-	-	-	-	-	-	210
Margin from credit-granting activities*	543	19	1	1	203	18	4	789
activities*	122	-	-	-	21	15	2	160
Total net interest income	665	19	1	1	224	33	6	949
Balance of credit to the public	14,300	903	28	81	6,730	957	300	23,299
Balance of deposits of the public	17,882	-	-	-	4,150	666	132	22,830

Small Business Segment (continued):

						Overseas activity		
	Banking and finance	Credit cards	Capital market	Mortgages	Real estate	Banking and finance	Real estate	Total
	2012							
	NIS millions							
Net interest income:								
From external sources	724	24	1	4	298	39	7	1,097
Intersegmental	(59)	(6)	(1)	(3)	(92)	(9)	(3)	(173)
Non-interest income:								
From external sources	339	108	23	-	66	14	1	551
Intersegmental	3	(47)	-	-	-	-	-	(44)
Total income	1,007	79	23	1	272	44	5	1,431
Expenses in respect of credit losses	74	-	-	-	7	3	-	84
Operating and other expenses:								
To external sources	649	52	12	-	109	29	3	854
Intersegmental	1	3	-	-	-	-	-	4
Profit before taxes	283	24	11	1	156	12	2	489
Provision for taxes on profit	100	7	4	-	55	1	-	167
Profit after taxes	183	17	7	1	101	11	2	322
Net profit attributable to non-controlling interests	(1)	(2)	-	-	-	-	-	(3)
Net profit (loss)	182	15	7	1	101	11	2	319
Return on equity								21.1%
Average balance of assets	13,105	840	24	101	5,876	668	174	20,788
Average balance of credit to the public	13,099	827	24	98	5,872	668	174	20,762
Average balance of liabilities	14,907	1,430	-	-	3,282	528	66	20,213
Average balance of deposits of the public	14,848	-	-	-	3,163	528	66	18,605
Average balance of risk assets	10,993	665	23	75	5,810	669	174	18,409
Average balance of mutual funds and supplementary training funds	-	-	2,175	-	-	-	-	2,175
Average balance of securities	-	-	4,748	-	-	5	-	4,753
Average balance of other assets under management	226	-	-	-	-	-	-	226
Margin from credit-granting activities*	519	18	-	1	182	16	3	739
Margin from deposit-taking activities*	146	-	-	-	24	14	1	185
Total net interest income	665	18	-	1	206	30	4	924
Balance of credit to the public at 31 December 2012	13,470	874	29	107	6,137	883	233	21,733
Balance of deposits of the public at 31 December 2012	15,505	-	-	-	3,482	622	57	19,666

Main changes in the volume of activity

Credit in the small business segment increased by NIS 1.6 billion, 7.2%, most of which was in respect of activity in Israel. Deposits of the public increased by NIS 3.2 billion, 16.1%,, the increase deriving from domestic activity.

Main changes in the net profit

Net profit in the small business segment totaled NIS 288 million in 2013, compared with NIS 319 million in 2012.

The decrease in profit derives mainly from an increase in expenses in respect of credit losses amounting to NIS 28 million, as a result of an increase in expenses in the Bank and in the United Kingdom overseas unit and from an increase in operating expenses of NIS 73 million. The decrease was partially offset by an increase in income of NIS 64 million.

Net profit in the small business segment in Israel amounted to NIS 284 million in 2013, compared with a profit of NIS 306 million in 2012. Net profit from foreign activity in 2013 amounted to NIS 4 million, compared with NIS 13 million in 2012. The decrease in profit was mainly in respect of an increase in expenses in respect of credit losses in the overseas units in the United Kingdom and Romania.

3. Corporate Banking Segment

General

The corporate banking segment specializes in providing banking and financial services to large corporations, some of which are corporations with multi-national activities, and customers whose main occupation is in the fields of construction and real estate/infrastructure projects. The customers belonging to this segment are characterized by their leading position in the market and dominance in their sphere of business. The services provided are based on the provision of an overall solution for all of the customer's needs, with a view to the entire range of their business activity, *inter alia*: various types of credit, financing and international trade, investment services, capital market activities, financial instruments designed to hedge against market risks, complex transactions (projects, mergers and acquisitions, syndicate organization), etc. Services outside of Israel are provided to the corporate segment through the Bank's overseas units - Bank Leumi USA, Bank Leumi (UK) and Bank Leumi Romania.

Structure of the segment

The corporate banking segment is managed in Israel by the Corporate and Commercial Division and the International Credit and Real Estate Division and is dealt with by Corporate Department and the Construction and Real Estate Department, which together operate seven corporate sectors. Service to customers is provided by customer relations managers, who coordinate the Group's services to the customer and specialize in the market sector in which the customer operates. The segment supplies a comprehensive range of banking services to all types of companies in the various sectors. The customers' accounts are mainly managed through departments located in central branches, which specialize in handling large customers and customers with diverse activities, as well as through the Bank's overseas offices. Special/complex transactions, for example, international trade activity, finance of foreign debtors/domestic debtors, sale of debts and syndicates, etc., the acquisition of means of control, examination of investment programs and the financing of projects are handled by designated units specializing in handling transactions of this kind, due to the complexity and level of risk involved.

The Special Loans Unit, which operates within the framework of the segment, deals with corporate customers who have encountered difficulties, with experience in assisting in the recovery of active customers and the collection of debts of corporate customers who cannot be rehabilitated.

The sectors in the Corporate Department are as follows:

a. The technology sector, specializing in providing services to corporate customers, mainly in the area of high-tech, communication and the security industry;

b. The consumption and trade sector, specializing in providing services to corporate customers, mainly in the area of the food and drink industry, hotels, the written media, retail chains, importers of household appliances, importers of agricultural, wood and metal products;

c. The industry, transport and public institutions sector, specializing in providing services for corporate customers, mainly from the area of industry, airline companies, vehicle importers, leasing, aircraft and local authorities;

d. The chemicals sector, energy and holding companies, specializing in providing services for holding companies and corporate customers, mainly from the area of chemicals, pharmaceuticals, energy and fuel companies.

e. The construction company sector, providing a wide range of banking services for large customers in the sector in the field of construction and real estate in Israel and abroad.

f. The real estate initiation sector, specializing in the provision of services to corporate customers, including middle-market, whose main activity is financing the residential sector, which is dealt with using the construction loan method.

g. The infrastructure sector, which is engaged in the financing of national infrastructure projects using the public private partnership method which is based on cooperation between the public and private segments and in providing services to corporate customers in the field of performance and infrastructure contracting.

Business objectives and strategy

The following information is "forward-looking information." For the meaning of this term, see above in the chapter, "Description of the Banking Corporation and Forward-Looking Information".

The main objective of this segment is to deepen its relative advantage, provide maximum service to the Department's customers and to continue to improve its contribution to the Group’s profits, through careful and prudent scrutiny of the exposures deriving from customers' activity and the unique risks for this sector. At the same time, the division acts to expand the variety of products and services being offered to customers.

In light of the slowdown in corporate activity which occurred in 2013, the segment continued with the implementation of considered credit policy, distinguishing between the various risk levels, and the determination of credit margins and its terms, respectively.

The financing of corporate activity in the Bank's main service centers contributes to the dispersal of risks through exposure to various macroeconomic environments of customers.

In March 2013, a decision was taken to close the Bank's Diamond Stock Exchange branch. The implementation of the decision commenced on the date the decision was made, and it will continue in 2014. In addition, at the beginning of 2014, the Bank decided on the closure of the activity of the Diamonds and Jewelry Department in the Bank's overseas unit in New York, which will take place during 2014-2015.

Restrictions, legislation, standards, and special constraints applicable to the segment

The restrictions that are especially relevant for the corporate banking segment are the restrictions on the amount of indebtedness of large borrowers and groups of borrowers prescribed in Proper Conduct of Banking Management Regulation No. 313 and the restriction in accordance with Proper Conduct of Banking Business Regulation 323 relating to the balance of credit for all transactions for purchase of the means of control.

For further information, see the chapter, "Exposure to Risk and Methods of Risk Management", section, "Credit Concentrations".

According to Proper Conduct of Banking Business Management Regulation no. 315, when the total indebtedness of a certain sector to a banking corporation exceeds 20% of the total indebtedness of the public to a banking corporation (on an unconsolidated basis), the excess is considered a departure for the purpose of concentrations of sector indebtedness. In this case, it is necessary to make an additional allowance for credit losses in respect of the amount of the excess.

The rate of concentrations in the Bank to the various sectors (including real estate) at the end of 2013 is at the regulatory limit.

In the Real Estate Department, the financing of the projects in the construction loan format relies upon, inter alia, the existence of an operating system for the deposit of payments from purchasers of housing units in projects being supported on the basis of the coupon method, and the taking out of sale guarantees with a consistent wording, in accordance with the legislation and the directives of the Bank of Israel.

Developments in markets of the segment or changes in the characteristics of its customers

The following information is "forward-looking information". For the meaning of this term, see above in the chapter, "Description of the Banking Corporation and Forward-Looking Information".

2013 was characterized by a decline in demand for corporate banking credit, against a background of a slowdown in business activity and by a paucity of large financial transactions.

Expectations for 2014 are for a continuation of moderate economic growth in Israel and around the world, which will have repercussions both for export customers and for customers operating in the domestic market. Corporate activity will be affected by the macroeconomic situation, for example, the recovery of growth in the United States and Europe, the appreciation of the shekel and other macro data, which will impact the investment decisions of the large companies in the Israeli economy.

In view of this, the corporate segment manages credit risk with extreme caution, routinely examining the population of customer, focusing on the sensitive customers and the examination of the development trends and the implications thereon.

2013 was characterized in the real estate area by lively activity in the housing market, retaining a similar risk level to 2012, and the continuation of government/regulatory intervention, against a background of the price of housing which continued to rise (although at a moderate rate compared with past periods).

The office rental property market, which serves the corporate segment and is in a high correlation with growth in the corporate product, and the commercial real estate market which is strongly affected by developments in private household consumption, retained relative stability throughout the year, which, at this stage, is reflected in maintaining high occupancy rates and stable rents. Stability was also identified in the field of national infrastructure, in which the moderate growth continued in national projects, and in the area of performance and infrastructure, which, in recent years, has enjoyed an increase in the volume of housing and non-housing construction in recent years.

In 2014, activity in the area of real estate is expected to be affected by the macroeconomic situation, the government/regulatory intervention (particularly in the housing market), building completions (particularly in the office market) and the volumes of investments by the State in the area of national infrastructure.

For further information, on the subject of the world economy, see the chapter, "Principal Developments in the Economy".

Technological changes that may have a material impact on the segment

The information systems that serve the corporate banking segment are intended to assist in analyzing customers' needs and in the ongoing work with them, in the analysis and measurement of credit risks and borrowers' assessments and in the monitoring and control of customers' activities. The various technological systems are updated and upgraded on an ongoing basis for the benefit of the segment.

Critical success factors in the segment

Critical success factors in the segment are: staff possessing high levels of management, professional and interpersonal abilities (both *vis-à-vis* the customers and within the organization), familiarity with the customers, including their financial position and the prospects/risks inherent in working with them. In addition, recognizing the various segments of the market and monitoring the changes occurring in the market in order to identify potential and avoid risk, a high degree of skill in planning complex financing packages, proper management and control on supporting projects, constant investment in technological aids, and diligence in supplying service and providing solutions to customers' banking needs within suitable response times, credit risk management and control.

Alternatives to the products and services of the segment, and the changes that have occurred therein

In recent years, the involvement of the capital market has been increasing – whether through the issue of debentures or by the extension of direct loans by the institutional entities.

Since the sources available to the Bank for providing long-term financing are limited in comparison with the sources available in the short to medium-term, the Bank is taking steps in the area of the financing of projects and long-term investments (particularly, infrastructure projects and rental property) to bring in institutional investors and other banks to participate in financing these projects through their integration in financing consortia.

Products and services of the segment

The services provided include, *inter alia*, ongoing financing according to the customers' needs, financing of investments to maintain and expand operations, provision of solutions in the spheres of financing and international trade (including financing credit insurance or private insurance companies of projects abroad), financing and guidance of national and international projects, financing of mergers and acquisitions, organization of syndicates, financial instruments to hedge against currency risks, interest risks and fluctuations in commodities prices. The service also includes the initiation and promotion of banking services to the managements and employees of companies in the segment.

Finance in the area of construction and real estate was effected by the use of specific analysis and monitoring tools which assist in the decision-making process and control of financial support given to the various projects and assets. Financing was effected, directing the diversity of the credit portfolio and distinguishing between the various segments – housing, rental property with a designation for commerce and offices, construction financing of terrorism industry and commerce. The financing of housing projects will, in general, be effected using the construction loan method which facilitates close supervision of the high frequency on the lender's project.

Financing the area of construction and real estate also includes the special funding format for national infrastructure projects using the various types of the public private partnership (PPP) method. Analysis of these transactions and the construction of the appropriate financing package are carried out taking into account the nature of the project, an analysis of the ability to service the debt, the extent of right of recourse to promoters, the establishment and operation contract restriction and technical limits, etc.

In addition, pursuant to the financing of the area of construction and real estate, the department also deals with the extension of credit, support of the initiation and development of real estate and hotel projects and the purchase of rental properties through the Bank's overseas units.

Customers

Customers belonging to this sector are mostly characterized by their leading position in the market and dominance in their field of activity. Some of these companies public companies from a variety of different sectors of the economy, with complex organizational structures comprised of numerous management echelons and a broad span of control.

Marketing and distribution

Service and marketing to customers are provided by customer relations managers who specialize in the sector of the economy in which the customers operate, and who coordinate the Group's services to customers.

Structure of competition in the segment and the changes that have occurred therein

The status of the Israeli banks as the sole financers of corporations has continued to dwindle over the years, so that the weighting of credit to the corporate sector (including small businesses) provided by the banking system stood at some 50% in the second half of 2013.

There is competition in the segment, both on the part of the four largest banking groups in Israel, and on the part of the smaller banks in the system.

However, the Israeli capital market and the institutional entities, such as insurance companies and pension funds, make up most of the competition for business credit (particularly for large companies). In recent years, there has been a greater involvement from the institutional entities, and, as a consequence, the percentage of direct loans extended by institutional corporate entities has continued to increase.

Human Capital

In order to bring employees engaged in the field of credit to the required professional level, there is an appropriate training system. On specific topics, there is the support of a specialist or outside unit (for example, appraisal experts, team of accounts, project support unit for financing international trade, mergers and acquisitions, unit for financing syndicate participation, etc.).

In 2013, the average number of positions assigned to the segment (including the International Credit and Real Estate Division) totaled 1,034 positions, of which, 429 were management positions, compared with 1,103 positions in 2012, 439 of which were management staff. Most of the employees have an academic education. In addition to their educational qualifications, as part of their training at the Bank, the employees undergo regular professional training in various fields of banking, as well as management courses. Within the scope of their work, employees must possess the ability to analyze complex credit applications, to lead complicated transactions, and the ability to provide service of the highest standard.

Below is a summary of the results of operations of the Corporate Banking segment:

					Overseas activity		
	Banking and finance	Credit cards	Capital market	Real estate	Banking and finance	Real estate	Total
	2013						
	NIS millions						
Net interest income:							
From external sources	**1,519**	**24**	**-**	**985**	**(1)**	**1**	**2,528**
Intersegmental	**(675)**	**(5)**	**-**	**(487)**	**21**	**2**	**(1,144)**
Non-interest income:							
From external sources	**196**	**194**	**16**	**176**	**6**	**1**	**589**
Intersegmental	**52**	**(92)**	**(1)**	**98**	**-**	**-**	**57**
Total income	**1,092**	**121**	**15**	**772**	**26**	**4**	**2,030**
Expenses in respect of credit losses	**(36)**	**(2)**	**-**	**(128)**	**-**	**-**	**(166)**
Operating and other expenses:							
To external sources	**399**	**80**	**7**	**185**	**13**	**3**	**687**
Intersegmental	**-**	**1**	**-**	**-**	**-**	**-**	**1**
Profit (loss) before taxes	**729**	**42**	**8**	**715**	**13**	**1**	**1,508**
Provision for (benefit from) taxes	**261**	**11**	**3**	**259**	**3**	**-**	**537**
Profit (loss) after taxes	**468**	**31**	**5**	**456**	**10**	**1**	**971**
Net profit attributable to non-controlling interests	**-**	**(6)**	**-**	**-**	**-**	**-**	**(6)**
Net profit (loss)	**468**	**25**	**5**	**456**	**10**	**1**	**965**
Return on equity							**11.8%**
Average balance of assets	**42,647**	**393**	**166**	**23,104**	**232**	**92**	**66,634**
Average balance of credit to the public	**41,007**	**367**	**166**	**23,037**	**232**	**92**	**64,901**
Average balance of liabilities	**18,031**	**2,780**	**-**	**5,472**	**1,102**	**163**	**27,548**
Average balance of deposits of the public	**16,520**	**-**	**-**	**4,907**	**1,102**	**163**	**22,692**
Average balance of risk assets	**66,244**	**406**	**166**	**23,507**	**314**	**92**	**90,729**
Average balance of mutual funds and supplementary training funds	**-**	**-**	**2,366**	**-**	**-**	**-**	**2,366**
Average balance of securities	**-**	**-**	**59,059**	**-**	**62**	**-**	**59,121**
Average balance of other assets under management	**212**	**-**	**-**	**-**	**-**	**-**	**212**
Margin from credit-granting activities	**830**	**19**	**-**	**483**	**3**	**1**	**1,336**
Margin from deposit-taking activities	**14**	**-**	**-**	**15**	**17**	**2**	**48**
Total net interest income	**844**	**19**	**-**	**498**	**20**	**3**	**1,384**
Balance of credit to the public	**38,504**	**328**	**166**	**21,446**	**158**	**44**	**60,646**
Balance of deposits of the public	**16,523**	**-**	**-**	**5,364**	**767**	**162**	**22,816**

Corporate Banking Segment (continued)

	Banking and finance	Credit cards	Capital market	Real estate	Overseas activity: Banking and finance	Overseas activity: Real estate	Total
	2012						
	NIS millions						
Net interest income:							
From external sources	1,560	28	3	1,139	8	6	2,744
Intersegmental	(586)	(9)	(3)	(612)	14	-	(1,196)
Non-interest income:							
From external sources	102	189	15	297	8	2	613
Intersegmental	150	(100)	-	(26)	-	-	24
Total income	1,226	108	15	798	30	8	2,185
Expenses in respect of credit losses	991	1	-	(59)	-	-	933
Operating and other expenses:							
To external sources	375	76	17	160	18	4	650
Intersegmental	-	1	-	-	-	-	1
Profit (loss) before taxes	(140)	30	(2)	697	12	4	601
Provision for (benefit from) taxes	(52)	7	(1)	246	3	1	204
Profit (loss) after taxes	(88)	23	(1)	451	9	3	397
Net profit attributable to non-controlling interests	(1)	(4)	-	-	-	-	(5)
Net profit	(89)	19	(1)	451	9	3	392
Return on equity							4.3%
Average balance of assets	49,588	416	165	25,793	495	167	76,624
Average balance of credit to the public	47,320	393	165	25,700	495	167	74,240
Average balance of liabilities	20,981	2,676	-	5,574	879	170	30,280
Average balance of deposits of the public	18,780	-	-	5,168	879	170	24,997
Average balance of risk assets	76,624	393	164	26,195	618	167	104,161
Average balance of mutual funds and supplementary training funds	-	-	2,087	-	-	-	2,087
Average balance of securities	-	-	56,814	-	130	-	56,944
Average balance of other assets under management	226	-	-	-	-	-	226
Margin from credit-granting activities	949	19	-	508	3	5	1,484
Margin from deposit-taking activities	25	-	-	19	19	1	64
Total net interest income	974	19	-	527	22	6	1,548
Balance of credit to the public at 31 December 2012	44,452	389	166	24,649	392	204	70,252
Balance of deposits of the public at 31 December 2012	19,748	-	-	4,989	1,373	171	26,281

Main Changes in the Volumes of Activity

In the corporate banking segment, there was a decrease in credit to the public of some NIS 9.6 billion, 13.7%, primarily from domestic banking and financial activities. There was a decrease in deposits of the public of some NIS 3.5 billion, 13.2%, mainly in activity in Israel.

Main Changes in the Net Profit

Net profit in the corporate banking segment in 2013 totaled NIS 965 million, compared with NIS 392 million in the corresponding period in 2012, an increase of 146.2%. The increase in profit derived mainly from income in respect of credit losses amounting to NIS 166 million, which were recorded in 2013, compared with expenses in respect of credit losses amounting to NIS 933 million which were recorded last year, due to a reduction in the collective allowance and an increase in the collection of debts.

4. Commercial Banking Segment

General

Commercial banking specializes in the provision of the entire spectrum of financial services to middle-market business entities in all sectors of the economy. The interested parties of the business companies, including shareholders and senior office holders are also dealt with in this segment.

Service and marketing to these customers are carried out on an individual basis, including the financing of transactions with credit instruments tailored to the customers' unique requirements, the adaptation of investment products and financial instruments for hedging risks, the financing of international trade transactions, the financing of active customers in the capital market and start-up companies.

The commercial banking segment also includes activities outside of Israel through the Bank's subsidiaries abroad. Companies that are served by the Commercial Department leverage their relations with the Bank in Israel in order to expand their activities abroad. Banking services abroad, including the provision of credit lines to finance international trade, real estate purchases, and company mergers, are available to companies mainly through Bank Leumi USA, Bank Leumi (UK) and Bank Leumi Romania. The subsidiaries in the United States, the UK and Romania view the ongoing servicing of these companies as a direct continuation of the banking activities in Israel.

For further details about the overseas units, see below in the chapter, "Principal Investee Companies".

Structure of the segment

The segment is managed in Israel by the Commercial Department, which is a part of the Commercial Business Division. The Commercial Department is a unique organizational structure in the Israeli banking system, which enables it to provide its customers with all-inclusive and comprehensive service (a one-stop shop) and affords the Division a competitive edge. The principal contact with customers is through designated commercial branches located throughout the country. The Commercial Department has a sub-division main branch in Tel Aviv and 23 business branches located in industrial zones and in the major cities, which are attributed geographically to four commercial districts. The branches specialize in the management of business activities characteristic of the segment's customers, giving the Department a competitive advantage.

Goals and business strategy and expectations for developments in the coming year

The following information is "forward-looking information." For the meaning of this term, see above in the chapter, "Description of the Banking Corporation and Forward-Looking Information".

Commercial banking serves middle-market business customers. The strategic objective of commercial banking is to continue to strengthen its competitive advantage by expanding the activities with existing customers and by recruiting new customers, placing an emphasis on financing customers characterized by potential for growth and an appropriate level of risk, while providing comprehensive solutions for the benefit of its customers operating in Israel and abroad. One of the strategic focuses is strengthening the Leumi's advantage and leadership in the field of hi-tech, leveraging the expertise and professionalism of the hi-tech teams in the Commercial Department in conjunction with Leumi Tech

Restrictions, legislation, regulations and special constraints that apply to the segment

See details above in the chapter. "Regulation, General Environment and Effect of External Factors on Activity"

Developments in the markets of the segment, and in its customers' characteristics

The main activities of the segment's customers are in the local market, in the industrial, infrastructure, trade and services and real estate sectors of the economy and markets abroad, either directly or through subsidiaries.

Expectations for 2014 are for continuation of moderate economic growth around the world and in Israel which is expected to have implications for export customers and customers active in the domestic market. Accordingly, the Commercial Department is taking particularly cautious steps in risk management, regularly reviewing the customer population, and, in particular, sensitive customers, in particular, and reviewing trends of developments and their implications.

Technological changes

- The segment's employees are assisted by computerized systems that support various processes carried out in the segment, such as control, definition and measurement of targets, marketing and business development.
- The segment supplies its customers with technological tools, similar to those used by all of the Bank's customers, through, among other things, a business portal, which expands the range of services for the convenience of the corporate customer. The Bank continues striving to develop these systems in order to respond to the changing and developing needs of the segment's customers.

Critical success factors in the segment

- Identifying the customer's needs and adapting appropriate inclusive solutions, while reducing response time and raising the standards of service.
- Familiarity with the customer, including his financial position and the prospects/risks inherent in working with him, as a basis for optimal risk management.
- Cultivating human capital and constantly raising its professional level at the required pace, in light of the changes in the capital market and the business environment.
- Maintaining a control system to reduce the credit risks and a strict approach in relation to all matters pertaining to compliance.

Main entry and exit barriers in the segment

- Training professional manpower with diverse skills.
- Maintaining a range of products tailored to the customers' needs.
- Establishing a network of distribution channels whose spread corresponds to the business potential.
- Establishing and developing technological means to serve customers and employees.

Competition

Competing parties in this segment of activity, in both the credit and investments spheres, are all of the banks operating in Israel (domestic and foreign), overseas banks, entities operating in the capital market, and insurance companies. The insurance companies compete for customers in the segment in both the credit sphere and the investment services sphere, while private investment houses are competitors in the investments sphere. The intensity of the competition that the Bank has been facing in the commercial banking segment in recent years from all factors has growing stronger.

Human Capital

- The average number of positions assigned to the segment in 2013 totaled 1,844 of which 769 were management positions, compared with 1,899 positions in 2012, 779 of which were management staff positions.

- The branches and the headquarters are staffed mainly by employees and managers who are all university graduates. In addition, the employees and managers have undergone professional training in the management of the business activities related and adapted to the Department's customers.

Below is a summary of the results of operations of the Commercial Banking Segment:

	Banking and finance	Credit cards	Capital market	Real estate	Overseas activity: Banking and finance	Overseas activity: Capital market	Overseas activity: Real estate	Total
	2013							
	NIS millions							
Net interest income:								
From external sources	583	10	-	357	571	-	135	1,656
Intersegmental	20	(2)	-	(162)	(87)	-	(46)	(277)
Non-interest income:								
From external sources	223	78	45	62	70	7	7	492
Intersegmental	125	(34)	(4)	(4)	-	-	-	83
Total income	951	52	41	253	554	7	96	1,954
Expenses in respect of credit losses	(27)	(1)	-	(1)	89	-	126	186
Operating and other expenses:								
To external sources	551	34	39	66	342	4	39	1,075
Intersegmental	-	1	-	-	-	-	-	1
Profit (loss) before taxes	427	18	2	188	123	3	(69)	692
Provision for (benefit from) taxes	155	5	1	68	58	1	(11)	277
Profit (loss) after taxes	272	13	1	120	65	2	(58)	415
Net profit attributable to non-controlling interests	-	(3)	-	-	-	-	-	(3)
Net profit (loss)	272	10	1	120	65	2	(58)	412
Return on equity								9.0%
Average balance of assets	24,511	357	258	8,184	14,985	-	3,047	51,342
Average balance of credit to the public	22,842	347	257	8,160	14,784	-	2,993	49,383
Average balance of liabilities	36,899	1,082	-	2,521	10,877	-	247	51,626
Average balance of deposits of the public	36,295	-	-	2,440	10,684	-	238	49,657
Average balance of risk assets	27,237	306	262	8,104	14,770	-	3,047	53,726
Average balance of mutual funds and supplementary training funds	-	-	5,005	-	-	148	-	5,153
Average balance of securities	-	-	45,120	-	-	1,532	-	46,652
Average balance of other assets under management	653	-	-	-	-	-	-	653
Margin from credit-granting activities	541	8	-	186	267	-	85	1,087
Margin from deposit-taking activities	62	-	-	9	217	-	4	292
Total net interest income	603	8	-	195	484	-	89	1,379
Balance of credit to the public	23,320	321	238	8,481	14,276	-	2,994	49,630
Balance of deposits of the public	38,792	-	-	2,666	10,206	-	214	51,878

Commercial Banking Segment (continued)

	Banking and finance	Credit cards	Capital market	Real estate	Overseas activity: Banking and finance	Overseas activity: Capital market	Overseas activity: Real estate	Total
	2012							
	NIS millions							
Net interest income:								
From external sources	512	12	12	364	582	-	138	1,620
Intersegmental	91	(4)	(12)	(169)	(88)	-	(47)	(229)
Non-interest income:								
From external sources	252	72	43	53	76	9	12	517
Intersegmental	75	(36)	-	-	-	-	-	39
Total income	930	44	43	248	570	9	103	1,947
Expenses in respect of credit losses	46	-	-	(4)	40	-	94	176
Operating and other expenses:								
To external sources	513	31	67	64	355	6	46	1,082
Intersegmental	(1)	1	-	1	-	-	-	1
Profit (loss) before taxes	372	12	(24)	187	175	3	(37)	688
Provision for (benefit from) taxes	131	4	(8)	66	64	1	(6)	252
Profit (loss) after taxes	241	8	(16)	121	111	2	(31)	436
Net profit attributable to non-controlling interests	-	(2)	-	-	-	-	-	(2)
Net profit	241	6	(16)	121	111	2	(31)	434
Return on equity								10.0%
Average balance of assets	23,578	321	237	8,311	15,467	-	3,282	51,196
Average balance of credit to the public	22,800	312	237	8,299	15,253	-	3,223	50,124
Average balance of liabilities	35,149	957	61	2,805	11,150	-	364	50,486
Average balance of deposits of the public	34,167	-	61	2,690	10,964	-	357	48,239
Average balance of risk assets	26,872	270	265	9,285	14,633	-	3,282	54,607
Average balance of mutual funds and supplementary training funds	-	-	3,790	-	-	157	-	3,947
Average balance of securities	-	-	40,809	-	-	2,110	-	42,919
Average balance of other assets under management	685	-	-	-	-	-	-	685
Margin from credit-granting activities	523	8	-	184	269	-	86	1,070
Margin from deposit-taking activities	80	-	-	11	225	-	5	321
Total net interest income	603	8	-	195	494	-	91	1,391
Balance of credit to the public at 31 December 2012	22,846	297	122	8,271	15,350	-	3,022	49,908
Balance of deposits of the public at 31 December 2012	35,889	-	-	2,751	11,162	-	306	50,108

Main Changes in the Volumes of Activity

Credit to the public fell by some NIS 0.3 billion, 0.6%. Deposits of the public increased by some NIS 1.8 billion, 3.5%, as a result of an increase in activity in Israel amounting to NIS 2.8 billion, which was partially offset by a decrease in overseas activity amounting to NIS 1.0 billion.

Main Changes in the Net Profit

Net profit in the commercial banking segment totaled NIS 412 million in 2013, compared with NIS 434 million in 2012, a fall of 5.1%.

The decrease in profit derives primarily from a decline in activity abroad amounting to some NIS 73 million, as a result of credit loss expenses amounting to NIS 81 million in the overseas units in the United States and United Kingdom. The decrease was offset by an increase in activity in Israel amounting to NIS 51 million, arising mainly from recording income in respect of credit losses amounting to NIS 29 million in 2013, as a result of an increase in the collection of debts, compared to expenses in respect of credit losses amounting to NIS 42 million in 2012.

5. Private Banking Segment

General

Private banking provides services to wealthy customers in Israel and worldwide. The activities are carried out through unique centers in Israel designated for foreign and Israeli residents, as well as through the Bank's subsidiaries in the United States, the United Kingdom, Switzerland, Luxembourg, Romania, Uruguay and Jersey. In addition, representative offices of the Group operate in Europe, Latin America, and Canada. Representative offices of Leumi Switzerland, Leumi Luxembourg and Leumi USA operate in Israel.

The structure of the segment

The private banking line is operated in Israel through the provision of exclusive and personal service by professional teams in seven unique centers around the country, who serve local residents and foreign residents in their **own** language, and who are familiar with the customers' needs, preferences and areas of interest.

Outside of Israel, private banking services are provided within the framework of the subsidiaries and representative offices

Goals and business strategy

The vision of private banking is to be "the private banking choice of customers as the leading private banker in Israel." This vision emphasizes a number of core values: focus on and attention to each existing and potential customer, the profitability of the customer's asset portfolio, to the level of professionalism and excellence in service, while developing professional and competitive teams with initiative, and the highest standards of service orientation.

Restrictions, legislation, regulations and special constraints that apply to the segment

The private banking segment in Israel operates within the context of laws, directives and regulations, which are imposed on the banking system in Israel by entities, such as the Banking Supervision Department in the Bank of Israel, the Commissioner of the Capital Market, Insurance and Savings, the Antitrust General Director, the Israel Securities Authority, the Authority for the Prohibition on Money Laundering and other entities. The Bank's overseas subsidiaries and representative offices operate by virtue of permits from the Banking Supervision Department in the Bank of Israel, and are also subject to local regulation.

In recent years, the Private Banking has undergone a process of adaptation to changes, both in regulation and in international enforcement. Like other banks, Bank Leumi is adapting to these changes.

For further information on the subject of FATCA, see above in the chapter, "Regulation, General Environment and the Effect of External Factors on Activities"

For further information regarding "American customers", see below in the chapter, "Legal Proceedings".

Developments in the markets of the operating segment, or changes in its customers' characteristics

Business reality is characterized by a high degree of uncertainty, increasing risk, fierce competitive conditions, with substantial changes in regulations, and with a shift in growth centers of global wealth to the east.

Technological changes

The private banking segment has at its disposal technology systems, which provide detailed reports to customers regarding their investments and assets and assists the counselors to better manage and monitor the customers' portfolios.

Currently, advanced new and dynamic websites are available for the benefit of customers, which assist in presenting the Bank and Group and its range of activities around the world. The information and the way in which it is presented are utilized as a premier level marketing tool *vis-à-vis* the customers and *vis-à-vis* the competition in Israel and worldwide.

Critical success factors in the private banking segment

- A range of comprehensive and advanced solutions and products for managing customers' assets and responding to their needs.
- Counseling of customers by a professional team supported by analysts and information systems.
- Provision of personal and customized VIP services, over and above routine financial services;

The main entry and exit barriers in the segment

- Training of skilled, qualified manpower possessing high levels of professionalism and service abilities.
- International spread of centers of activity throughout the world.
- Implementation of means of control over the entire range of activities.
- Establishment, maintenance and upgrading of advanced technological information systems.
- Offering a broad spectrum of financial products and services.

Marketing and sales promotion

The marketing objective is to increase the customer base while creating image differentiation, both within the Group and *vis-à-vis* the competition. In addition, the Bank takes steps to retain customers and increase the Bank’s share in the customers’ asset portfolio. Marketing the private banking segment is carried out through image advertising in the media and press aimed at an affluent target audience, as well as through customer events, professional conferences, sponsorships and collaborations with leading cultural and communal institutions in Israel and around the world, direct mailings and the Internet.

Competition

In the private banking segment, Leumi competes in Israel with Israeli banks and with local representative offices of foreign banks, which have the same customer targets. Overseas, the Bank competes with local banks and investment houses that offer private banking and investment services, as well as with branches and representative offices of Israeli banks.

Human capital

In 2013, the average number of positions assigned to the segment was 806 of which 419 were management positions, compared with 875 positions in 2012, of which 454 were management positions**.**

Employees of the private banking segment undergo comprehensive training, including wide-ranging professional and management training courses. In addition, the employees attend extensive workshops for acquiring high service skills.

Cooperation agreements

As stated, the private banking segment offers customers a broad range of products, within the framework of open architecture (reflected in cooperation with international entities). Through this cooperation, Leumi offers a range of advanced investment products constituting the main attraction for foreign resident investors – both existing and new – which consequently increases the volume of assets that they hold in the Group.

Below is a summary of the results of operations of the Private Banking Segment:

						Overseas activity				
	Banking and finance	Credit cards	Capital market	Mortgages	Real estate	Banking and finance	Capital market	Mortgages	Real estate	Total
	2013									
	NIS millions									
Net interest income:										
From external sources	(155)	-	-	1	6	40	-	37	(1)	(72)
Intersegmental	232	-	-	(1)	6	147	-	(23)	4	365
Non-interest income:										
From external sources	(27)	1	172	-	17	172	193	4	1	533
Intersegmental	63	1	(1)	-	1	13	-	-	-	77
Total income	113	2	171	-	30	372	193	18	4	903
Expenses in respect of credit losses	3	-	-	-	2	4	-	-	-	9
Operating and other expenses:										
To external sources	168	2	73	-	14	384	215	10	2	868
Intersegmental	1	1	-	-	-	1	1	-	-	4
Profit (loss) before taxes	(59)	(1)	98	-	14	(17)	(23)	8	2	22
Provision for (benefit from) taxes	(19)	-	33	-	5	10	2	2	-	33
Profit (loss) after taxes	(40)	(1)	65	-	9	(27)	(25)	6	2	(11)
Net profit attributable to non-controlling interests	-	-	-	-	-	(4)	-	-	-	(4)
Net profit (loss)	(40)	(1)	65	-	9	(31)	(25)	6	2	(15)
Return on equity										(1.6%)
Average balance of assets	1,439	65	31	43	646	8,782	-	858	-	11,864
Average balance credit to the public	1,328	65	31	43	638	4,146	-	858	-	7,109
Average balance of liabilities	18,804	-	6	-	1,426	16,481	-	17	150	36,884
Average balance of deposits of the public	18,563	-	6	-	1,419	16,070	-	17	151	36,226
Average balance of risk assets	1,763	48	31	25	607	6,511	-	300	-	9,285
and supplementary training funds	-	-	6,406	-	-	-	1,775	-	-	8,181
Average balance of securities	-	-	42,174	-	-	-	34,552	-	-	76,726
Average balance of other assets under management	188	-	-	-	-	-	-	-	-	188
Margin from credit-granting activities	18	-	-	-	8	47	-	14	-	87
Margin from deposit-taking activities	59	-	-	-	4	140	-	-	3	206
Total net interest income	77	-	-	-	12	187	-	14	3	293
Balance of credit to the public	1,225	68	31	48	789	3,476	-	818	-	6,455
Balance of deposits of the public	17,700	-	30	-	1,520	15,384	-	14	146	34,794

Private Banking Segment (continued):

						Overseas activity				
	Banking and finance	Credit cards	Capital market	Mortgages	Real estate	Banking and finance	Capital market	Mortgages	Real estate	Total
	2012									
	NIS millions									
Net interest income:										
From external sources	(199)	-	-	1	(4)	41	-	41	(2)	(122)
Intersegmental	324	-	-	(1)	15	155	-	(26)	5	472
Non-interest income:										
From external sources	(6)	1	164	-	12	228	201	5	1	606
Intersegmental	43	1	-	-	-	7	-	-	-	51
Total income	162	2	164	-	23	431	201	20	4	1,007
Expenses in respect of credit losses	(3)	-	-	-	-	4	-	-	-	1
Operating and other expenses:										
To external sources	173	2	68	-	12	414	211	12	2	894
Intersegmental	-	1	-	-	-	2	1	-	-	4
Profit (loss) before taxes	(8)	(1)	96	-	11	11	(11)	8	2	108
Provision for (benefit from) taxes	(1)	-	32	-	4	-	(6)	2	-	31
Net profit (loss)	(7)	(1)	64	-	7	11	(5)	6	2	77
Return on equity										7.9%
Average balance of assets	1,891	54	17	35	429	9,860	-	1,029	-	13,315
public	1,792	54	17	35	425	5,220	-	1,029	-	8,572
Average balance of liabilities	19,546	-	7	-	1,362	18,417	-	15	189	39,536
Average balance of deposits of the public	19,323	-	7	-	1,318	17,818	-	15	189	38,670
Average balance of risk assets	2,229	39	10	25	429	7,743	-	360	-	10,835
Average balance of mutual funds and supplementary training funds	-	-	4,953	-	-	-	1,715	-	-	6,668
Average balance of securities	-	-	40,193	-	-	-	36,810	-	-	77,003
under management	227	-	-	-	-	-	-	-	-	227
Margin from credit-granting activities	20	-	-	-	5	57	-	15	-	97
Margin from deposit-taking activities	105	-	-	-	6	139	-	-	3	253
Total net interest income	125	-	-	-	11	196	-	15	3	350
Balance of credit to the public at 31 December 2012	1,775	64	44	44	423	4,919	-	901	-	8,170
Balance of deposits of the public at 31 December 2012	19,361	-	-	-	1,407	17,379	-	15	176	38,338

Main changes in volume of activity in the segment

Credit to the public decreased by NIS 1.7 billion, mainly as a result of a decrease in credit in overseas activity, which was due the appreciation of the shekel against foreign currencies.

Deposits of the public fell by some NIS 3.5 billion, or 9.2%, both in activity in Israel and in activity overseas.

Changes in net profit

Net loss of the private banking segment in 2013 amounted to NIS 15 million, compared with at profit of NIS 77 million in the corresponding period in 2012, a decrease of NIS 92 million. The decrease in profit derives from a fall in income amounting to NIS 104 million, mainly due to a decrease in income from foreign activity amounting to NIS 69 million.

6. Financial Management Segment – Capital Markets

General

This segment centralizes the financial management of the Bank and of the Group and the management of the dealing room, coordinates the contacts, and provides various services to banks and institutional investors. The areas of activity of the segment are as follows:

- Management of the *nostro*, by way of the investment of the Bank's independent financial means in tradable and non-tradable investment instruments and management of direct investments, in the companies' tradable and non-tradable shares;
- Management of the dealing rooms, which provide trading services to customers of the Bank, primarily in currencies, securities and derivative instruments;
- Management of market risk exposures – including the management of basis, interest and liquidity exposures;
- Price management – by setting transfer prices and costing special financial transactions;
- Management of banking activity of customers that are institutional investors;
- Public and private issues of Leumi, including deferred notes and debentures;
- Development of financial instruments.

Structure and business strategy in the segment

The financial management activity is carried out by the Capital Markets Division and in the subsidiaries in Israel and abroad by the market risk managers in the subsidiaries. The activities include the Bank's dealing rooms, management of the *nostro*, and the provision of service to customers active in the capital and money markets, including institutional customers.

The segment's business strategy is based on the Group's capital adequacy policy and its policies for managing risks, including market risks and the *nostro*, while addressing the management of the current liquidity and durability under stress conditions, and the interest and financial margin policies. The business objectives of the financial management segment are to meet profit targets adapted to risk, with activities being conducted within the framework of restrictions on risk exposure set by the Board of Directors. In the context of implementing the business strategy, the Division develops advanced financial instruments, including structured products and innovative products in the dealing room, in collaboration with the Bank's other operating segments.

Legislative restrictions, regulations and special constraints that apply to the segment

The segment's activities are subject to laws, regulations and regulatory directives imposed on the banking system in Israel.

The Bank is subject to the supervision of various authorities, including: the Bank of Israel and the Banking Supervision Department, the Commissioner of the Capital Market, Insurance and Savings, the Antitrust General Director and the Israel Securities Authority. The Bank's overseas subsidiaries and representative offices operate by virtue of permits from the Banking Supervision Department, and are also subject to local regulations.

Profit of the segment

The segment's profit is mainly influenced by the *nostro* activities, the dealing rooms and ALM management, as well as the results of non-banking companies included on equity basis. The principal components of net profit are as follows:

- Results of market risk management, including the changes that have occurred in transfer prices. Income and expenses resulting from changes in transfer prices are attributed in full to the financial segment, to which all of the market risks from the other operating segments are also transferred.
- Results of capital management, including the raising of capital and offerings to the public.

- Profits/losses from the realization of securities and from provisions for declines in values of securities in respect of declines of a non-temporary nature, and from unrealized profits/losses from adjustments of securities for trading to market value.
- Adjustments of derivative instruments to market value;
- Effects of foreign currency/shekel exchange rate and consumer price index differentials, including adjustments from the translation of overseas investments, including the effects of related taxes;
- Income/expenses deriving from the investment for pension, jubilee and regular holiday reserves;
- Particular costs relating to pension liabilities;
- Profits of companies included on equity basis.

Operating expenses of the segment include mainly direct operating expenses, as well as indirect expenses involved in the management of market risks, management of the independent securities (the *nostro*) portfolios and management of the dealing rooms.

Principal developments in the segment

During 2013, at the same time as the contraction of foreign currency credit in Israel, the Bank increased the amount and the variety of foreign currency investments in capital markets around the world.

During 2013, the Bank continued in expanding the operating services granted by the Bank to the institutional customers, particularly in the operation of provident funds and mutual funds.

Critical success factors in the segment

The critical success factors in the segment are mainly human capital, supported by advanced computer systems, working in an efficient and flexible management framework of control and monitoring. Human capital, requiring managerial, analytical, professional and commercial abilities, in the area of capital markets in Israel and abroad. These abilities relate to both operations in the capital market and to activities with and in the service of customers. Professionalism and constant updating is required regarding financial innovations, and in developments with implications on the capital markets, together with concentrated efforts to provide a response to the needs of customers and working in the proper time-frames.

Customers

The customers belonging to this segment are the mutual funds, provident funds, training funds, pension funds, commercial banks and investment banks, as well as other customers operating intensively in the capital markets.

Competition

The Bank faces strong competition in the field of its activities in the capital market and brokerage from investment houses and domestic and foreign banks.

Human capital

In 2013, the average number of positions assigned to the segment was some 682 positions, of which 313 were management positions, compared with 662 positions in 2012, 303 of which were management staff positions. Most of the employees have academic qualifications and, in addition, the employees attend professional courses in various fields and management courses arranged by the Bank

Below is a summary of the results of operations of the Financial Management Segment – Capital Markets:

	2013	2012
	NIS millions	
Net interest income:		
From external sources	**(821)**	184
Intersegmental	**1,513**	198
Non-interest income:		
From external sources	**1,531**	845
Intersegmental	**(223)**	(245)
Total income	**2,000**	982
Expenses in respect of credit losses	**(52)**	(29)
Operating and other expenses:		
To external sources	**1,280**	1,762
Intersegmental	**50**	44
Profit (loss) before taxes	**722**	(795)
Taxes on (benefit from taxes on) the profit	**199**	(251)
Profit (loss) after taxes	**523**	(544)
Group share in losses of companies included on equity basis after effect of tax	**(297)**	(69)
Net profit attributable to non-controlling interests	**2**	-
Net profit (loss)	**228**	(613)

In 2013, the net profit of the segment amounted to NIS 228 million, compared with a loss of NIS 613 million in 2012. This segment includes the Group's share in the profits of companies included on equity basis.

The change is explained by the following factors:

a. An increase in income amounting to NIS 1,018 million deriving mainly from noninterest income amounting to NIS 708 million, as a result profits from the sale of shares and sale of loans.

b. A decrease in operating expenses amounting to NIS 476 million, deriving from a decrease in operating expenses that were not loaded on the other operating segments, mainly expenses and a provision for the U.S. customers amounting to NIS 161 million, and in respect of a decrease in the provision for early retirement of NIS 248 million.

c. Income in respect of credit losses amounting to NIS 52 million, compared to income amounting to NIS 29 million in 2012.

The increase was partially offset as a result of an increase in the Group's share in the losses of companies included on equity basis amounting to NIS 228 million.

Companies included on equity basis (non-banking) (presented in the financial management segment).

The operating results of the Group's real investments are presented in the financial management segment.

Total investments of the Leumi Group in companies included on equity basis totaled some NIS 1,689 million on 31 December 2013, compared with NIS 2,129 million on 31 December 2012.

Investments in the Shares of Companies included on Equity Basis (Table 13 (b) - Basel II):

	Balance sheet value			**Market value**		**Capital adequacy requirements**	
	NIS millions			NIS millions			
Name of Company	**31 December 2013**	31 December 2012	Change %	**31 December 2013**	31 December 2012	**31 December 2013**	31 December 2012
The Israel Corporation Ltd.	**1,137**	1,567	(27.4)	**2,526**	3,367	**102**	141
Others	**552**	562	(1.8)	*** -**	* -	**50**	51
Total	**1,689**	2,129	(20.7)	**2,526**	3,367	**152**	192

* Of which, NIS 207 million at 31 December 2013 and NIS 208 million at 31 December 2012 are quoted.

The Israel Corporation

The Bank holds 17.96% of the means of control in the Israel Corporation Ltd., which is considered a significant non-bank corporation pursuant to the Banking Law (Licensing), as amended via the Concentrations Law on 11 December 2013 (for this purpose, see "the Concentrations Law") in the chapter, "General Environment and the Effect of External Factors on Activities"). The Bank is obliged to reduce its holdings in the Israel Corporation to 10% by 11 December 2019.

The Israel Corporation has announced an examination of the split of its holdings, such that the Israel Corporation will continue to hold Israel Chemicals Ltd and Oil Refineries Ltd., while its remaining holdings will be transferred and held by all the shareholders in the Israel Corporation through a new company. The Bank is examining the impact of the split. For further information, see the financial statements of the Israel Corporation as at 31 December 2013.

At the end of July 2013, the Russian potassium producer, Uralkali, announced its withdrawal from the potassium marketing company, jointly owned by it and Belaruskali (BPC), through which the two producers, Uralkali and Belaruskali, will export their product outside of their countries. At the same time as the withdrawal notice, Uralkali also announced a change in its sales strategy and a switch to a policy of favoring quantity over price, taking full advantage of the company's production capacity. This announcement triggered a process of reduction in potassium prices in the markets and led to a deferral in the purchase of potassium by customers in expectation of further price decreases. In the fourth quarter, demand was renewed, the level of activity on the various markets returned to normal and prices stabilized.

On 19 March 2014, the Israel Corporation published an Immediate Report regarding the intention of a subsidiary, ICL, to register its shares for trading in New York. The board of directors of the Israel Corporation instructed the company's management to examine the possibility in connection with the shares of ICL – a financial (derivative-type) transaction or a sale amounting to up to 7% of the share capital of ICL held by the Israel Corporation.

The contribution of the companies included on equity basis to the Group in 2013 was negative, amounting to a loss of NIS 293 million, compared with a loss of NIS 67 million for the corresponding period in 2012. The decrease in the contribution to the Group's profit in 2013, comparison to 2012 arose from an increase in the losses of the Israel Corporation Ltd. ("the Israel Corporation").

The contributions of the companies to the Group's net profit (in NIS millions) are as follows:

	2013	2012	% change
The Israel Corporation Ltd.	**(340)**	(110)	-
Others	**47**	43	9.3
Total	**(293)**	(67)	-

The contribution of companies included on equity basis to other comprehensive income at 31 December 2013 is a profit of NIS 11 million.

Migdal Holdings and Finances Ltd.

During 2013, the Bank sold its entire holding in the share capital of Migdal Insurance and Financial Holdings Ltd.

7. "Others" Segment – This segment includes activities not attributed to other segments.

This segment includes the other activities of the Group, each of which does not meet the criteria to be considered a profit segment, pursuant to the directives of the Bank of Israel.

This activity mainly includes a portion of the activities of the capital market companies that is not attributed to other segments. The main companies are the part of Leumi Partners which does not belong to the financial management segment and Leumi Capital Market Services.

The loss in the "other" segment in 2013 amounted to NIS 40 million, compared with a loss of NIS 125 million in 2012.

The following table presents a summary of the main changes, in NIS millions:

	2013	2012	Difference
Bank	**41**	20	21
Other companies in Israel	**13**	9	4
Companies abroad	**10**	10	-
Tax adjustments (1)	**(104)**	(164)	60
Total	**(40)**	(125)	85

(1) Tax differentials between the tax calculations in the segments and the effective tax in the consolidated financial statements.

Activities in Products

A. Capital market activities

The Group’s activities in the capital market include investment and pension counseling activities, brokerage in the securities and financial instruments market, including activity carried out through the foreign currency dealing rooms and the Israeli and foreign securities dealing rooms, brokerage and custodial and sub-custodial services, and banking and financial services to entities active in the capital market. A subsidiary of Leumi Partners Ltd., Leumi Partners Underwriters Ltd. engages in underwriting and the distribution of private and public offerings. Net profit in capital market activity amounted to NIS 86 million, compared to NIS 113 million in the corresponding period in 2012, a decrease in net profit of NIS 27 million, deriving mainly from an increase in operating expenses amounting to NIS 41 million.

The following table presents data on the activities in the capital market as presented in the various operating segments, including the activities of customers in the capital market, and the results of Leumi Partners Underwriters:

	Households	Small businesses	Corporate banking	Commercial banking	Private banking	Financial management and Others	Overseas activities	Total
	2013							
	NIS millions							
Net interest income	**3**	**1**	**-**	**-**	**-**	**5**	**-**	**9**
Noninterest income	**434**	**26**	**15**	**41**	**171**	**126**	**205**	**1,018**
Total income	**437**	**27**	**15**	**41**	**171**	**131**	**205**	**1,027**
Operating and other expenses	**381**	**16**	**7**	**39**	**73**	**140**	**227**	**883**
Profit (loss) before taxes	**56**	**11**	**8**	**2**	**98**	**(9)**	**(22)**	**144**
Net profit (loss)	**35**	**7**	**5**	**1**	**65**	**(4)**	**(23)**	**86**

	Households	Small businesses	Corporate banking	Commercial banking	Private banking	Financial management and Others	Overseas activities	Total
	2012							
	NIS millions							
Net interest income	3	-	-	-	-	6	-	9
Noninterest income	456	23	15	43	164	85	212	998
Total income	459	23	15	43	164	91	212	1,007
Operating and other expenses	314	12	17	96	68	114	221	842
Profit (loss) before taxes	145	11	(2)	(53)	96	(23)	(9)	165
Net profit (loss)	93	7	(1)	(34)	64	(13)	(3)	113

B. Credit cards - Leumi Card

Leumi Card Ltd. is a credit card company which is engaged in issuing and clearing credit cards and developing payment solutions and financial products. The company was established on 15 February 2000 and commenced business activity on 15 May 2000.

Issuance segment – Leumi Card issues cards under the brand names, Visa and Mastercard, through which businesses in Israel and around the world that honor these brands may be paid. Leumi Card, Bank Leumi and Arab Israel Bank Ltd. jointly issue the credit cards to their customers. In addition, the company issues credit cards to customers of all of the banks ("non-bank customers"), mostly with business entities.

Clearing segment – Leumi Card clears the Visa, Mastercard and Isracard brands through a joint interface which is operated through Automated Bank Services Ltd. ("ABS"). The clearing of Isracard cards by Leumi Card was made possible in May 2012, pursuant to Amendment no. 18 of the Banking Law (Licensing), 1981.

Clearing services include securing payment against vouchers for transactions made by credit card in exchange for a commission collected from a business. In addition, the company offers credit products and financial solutions to businesses, loans, discounting of vouchers and advancing payments.

In 2013, Leumi Card continued offering its customers a range of services and financial solutions.

The number of valid cards held by customers of the company at the end of 2013 amounted to 2.2 million, compared with 2.0 million at the end of 2012, an increase of 7%.

The total issuance turnover in 2013 amounted to NIS 60.4 billion, compared to NIS 55.8 billion in the corresponding period last year – an increase of 8%.

Pursuant to data from the Central Bureau of Statistics, the growth rate of volumes of credit card purchases in 2013 was 5.6% at fixed rates, compared to 6.7% in 2012.

On 20 December 2011, the Supervisor of Banks published the names of the companies who are "issuers with a wide scope of activity", as this term is defined in the Banking Law (Licensing). According to this announcement, each of the credit card companies currently operating in Israel: the Company, IsraCard and Cal were defined as "issuers with a wide scope of activity". Pursuant to this announcement, with effect from May 2012, the clearing of credit cards of IsraCard by credit card companies apart from IsraCard was permitted.

On 17 April 2012, a license agreement was signed by Leumi Card and Isracard, by virtue of which Leumi Card was granted a clearing and issuing license and the option for providing services for debit cards under the brand name of Isracard (hereinafter: "the License Agreement"). The agreement came into force on 15 May 2012. Further to the license agreement, the activity of clearing the cards under the Isracard brand is expected to be conducted in a similar fashion to the clearing of cards in the joint interface between credit card companies in the sector for clearing Visa and Mastercard cards.

On 13 September 2012, the Antitrust Commissioner granted a fixed exemption to the License Agreement. It was made dependent on a number of conditions, inter alia, it was provided that Isracard would not be able to collect the rate of license fees established between it and the company in the License Agreement, but rather a lower rate. In addition, as part of the conditions of the exemption, conditions were stipulated prohibiting the transfer of information between the companies, which is not for the purpose of implementing the agreements or which is not by virtue of the law or the exemption directive.

Like Mastercard Global, Isracard, has requested the Antitrust Court to issue an immunity injunction for the numerical data included in the Commissioner's exemption and the explanations on which it is based, and most of the rate of the license fees stipulated in the exemption. This request is pending in the Antitrust Court, which initially issued a temporary immunity injunction at the request of Isracard and Mastercard Global. On 11 February 2013, Isracard submitted a request to the Antitrust Court to approve a license agreement. In the request, Isracard claims that there is no justification for the Commissioner's determination and that the conditions agreed with Leumi Card and Cal should apply to the license agreement. On 27 January 2014, an evidentiary hearing was held, and on 5 February 2014, the parties summed up their arguments.

On 31 December 2013, the Supervisor of Banks published a final version of the regulatory framework for the grant of clearing licenses (for new entities requesting to be engaged in this field) by virtue of the Banking Law (Licensing). After completion of the requisite proceedings, it will be possible for additional entities in Israel to conduct credit card clearance activity through the receipt of a license from the Bank of Israel. The receipt of clearing activity by the new entities is expected to increase competition in the area of clearing.

Profitability

The income of Leumi Card, before operating, marketing, administrative and general expenses, totaled some NIS 987 million in 2013, compared with some NIS 954 million in 2012.

Leumi Card ended 2013 with a net profit of NIS 200 million, compared with NIS 180 million in 2012.

The following table presents data on credit card activities as presented in the various operating segments:

	Households	Small businesses	Corporate banking	Commercial banking	Private banking	Total
	2013					
	NIS millions					
Net interest income	**206**	**19**	**19**	**8**	**-**	**252**
Noninterest income	**679**	**73**	**102**	**44**	**2**	**900**
Total income	**885**	**92**	**121**	**52**	**2**	**1,152**
Expenses (income) in respect of credit losses	**13**	**(1)**	**(2)**	**(1)**	**-**	**9**
Operating and other expenses	**667**	**61**	**81**	**35**	**3**	**847**
Profit (loss) before taxes	**205**	**32**	**42**	**18**	**(1)**	**296**
Profit (loss) after taxes	**145**	**22**	**31**	**13**	**(1)**	**210**
Share of corporation in earnings of companies included on equity basis	**4**	**-**	**-**	**-**	**-**	**4**
Net profit attributable to non-controlling interests	**(27)**	**(4)**	**(6)**	**(3)**	**-**	**(40)**
Net profit (loss)	**122**	**18**	**25**	**10**	**(1)**	**174**

	Households	Small businesses	Corporate banking	Commercial banking	Private banking	Total
	2012					
	NIS millions					
Net interest income	201	18	19	8	-	246
Noninterest income	673	61	89	36	2	861
Total income	874	79	108	44	2	1,107
Expenses in respect of credit losses	18	-	1	-	-	19
Operating and other expenses	631	55	77	32	3	798
Profit (loss) before taxes	225	24	30	12	(1)	290
Profit (loss) after taxes	156	17	23	8	(1)	203
Share of corporation in profits of companies included on equity basis	2	-	-	-	-	2
Net profit attributable to non-controlling interests	(27)	(2)	(4)	(2)	-	(35)
Net profit (loss)	131	15	19	6	(1)	170

Interchange Fee

For information see note 18H(1) to the financial statements.

C. Construction and real estate

This activity includes the activity in the field of construction and real estate in the Bank's various operating segments.

The following table sets out data regarding construction and real estate activities, as presented in the various operating segments:

	Small businesses	Corporate banking	Commercial banking	Private banking	Overseas activity	Total
	2013					
	NIS millions					
Net interest income	**224**	**498**	**195**	**12**	**109**	**1,038**
Noninterest income	**78**	**274**	**58**	**18**	**14**	**442**
Total income	**302**	**772**	**253**	**30**	**123**	**1,480**
Expenses (income) in respect of credit losses	**21**	**(128)**	**(1)**	**2**	**127**	**21**
Operating and other expenses	**132**	**185**	**66**	**14**	**48**	**445**
Profit before taxes	**149**	**715**	**188**	**14**	**(52)**	**1,014**
Net profit (loss)	**95**	**456**	**120**	**9**	**(46)**	**634**

	Small businesses	Corporate banking	Commercial banking	Private banking	Overseas activity	Total
	2012					
	NIS millions					
Net interest income	206	527	195	11	115	1,054
Noninterest income	66	271	53	12	39	441
Total income	272	798	248	23	154	1,495
Expenses (income) in respect of credit losses	7	(59)	(4)	-	94	38
Operating and other expenses	109	160	65	12	55	401
Profit before taxes	156	697	187	11	5	1,056
Net profit	101	451	121	7	(3)	677

Profit centers in the Group

The following table presents details on the contribution of the Group's principal profit centers to the net operating profit:

	2013	2012	Change
	NIS millions		%
The Bank (4)	**1,775**	330	+
Consolidated companies in Israel (1)(4)	**556**	562	(1.1)
Consolidated companies abroad (2)	**(52)**	143	-
Companies included on equity basis (1)	**(332)**	(104)	-
Net operating profit	**1,947**	931	109.1
Profit of the subsidiaries abroad, in nominal terms (US$ millions) (3)	**18.9**	42.1	(55.2)

(1) Companies including on equity basis of subsidiaries in Israel were included in consolidated subsidiaries in Israel.
(2) Following particular adjustments to Israeli accounting principles.
(3) As reported by the subsidiaries abroad, including net profit to noncontrolling interest holders.
(4) The profits of Leumi Mortgage Bank in 2013 were included within the profits of the Bank. In 2012, NIS 303 million was included in the profits of subsidiaries in Israel.

Following are the principal changes in the contributions of the profit centers (after translation adjustments):

- The increase in net profit after taxes in the Bank derives from an increase in noninterest income, a decrease in respect of credit losses and a decrease in the rate of tax provision. Most of the explanations for the above changes are presented as part of the discussion on the Group's results in the chapter, "Development of Income, Expenses and Tax Provision" above.
- The decrease in the net operating profit of consolidated companies in Israel derives mainly an increase from the merger of Leumi Mortgage Bank at 31 December 2012, which was partly offset by an increase in the profits of Leumi Partners and Leumi Card.
- The loss of overseas subsidiaries arises mainly from an increase in respect of credit losses in the overseas units in the United Kingdom and the United States.
- The increase in the losses of companies included on equity basis arises mainly from an increase in the losses of the Israel Corporation.

The Bank

The increase in net operating profit is due mainly to:

- a decrease in expenses in respect of credit losses amounting to NIS 1,042 million.
- an increase in noninterest income amounting to NIS 645 million.
- a decrease in the rate of tax provision.

On the other hand, the increase in operating and other expenses amounting to NIS 139 million partially offset the above changes.

As mentioned above, the data of the Bank in 2012 do not include the effect of Leumi Mortgage Bank which, last year, was included within subsidiaries in Israel.

Subsidiaries in Israel

The decrease in net profit of consolidated companies in Israel is due mainly to the merger of Leumi Mortgage Bank on 31 December 2012 and the inclusion of its profits as a part of the Bank's profits, which was partially offset by the profits of Leumi Partners amounting to NIS 281 million, Leumi Card amounting to NIS 16 million.

Subsidiaries Abroad

The total contribution to profit of the overseas subsidiaries (excluding branches) as a convenience translation to U.S. dollars amounted to some US$ 18.4 million, compared with some US$ 42.1 million in the corresponding period last year. The overseas subsidiaries' contribution to net profit in shekels and with certain adjustments to Israeli accounting principles, amounted to a loss of NIS 52 million, compared with a profit of NIS 143 million in the corresponding period last year.

Companies included on equity basis

The income of companies included on equity basis comprises the results of a company included on equity basis, the Israel Corporation, and those companies of Leumi Partners. The increase in loss derives mainly from the losses of the Israel Corporation.

Activities according to the Group's Structure

The volume of activities in Israel rose in 2013 by 0.6%, and abroad, it fell by 9.7%.

Credit to the public in activities in Israel totaled some NIS 217.4 billion at the end of 2013, compared with NIS 214.7 billion at the end of 2012, an increase of 1.3%. Credit to the public in overseas activities totaled some NIS 23.5 billion at the end of 2013, compared with NIS 26.6 billion at the end of 2012, a decrease of 11.7%.

Deposits of the public in activities in Israel totaled some NIS 256.6 billion at the end of 2013, compared with NIS 256.2 billion at the end of 2012, an increase of 0.1%. Total deposits in overseas activities totaled some NIS 29.4 billion at the end of 2013, compared with NIS 33.3 billion at the end of 2012, a decline of 11.7%.

Information according to geographical regions*:

The following table presents principal data according to geographical regions (in NIS millions):

	Total Balance Sheet			Credit to the Public			Deposits of the Public		
	2013	2012	Change	**2013**	2012	Change	**2013**	2012	Change
Region			%			%			%
Israel	**338,142**	336,069	0.6	**217,381**	214,668	1.3	**256,586**	256,216	0.1
United States	**18,055**	20,103	(10.2)	**12,926**	13,985	(7.6)	**13,982**	16,336	(14.4)
United Kingdom	**9,272**	9,732	(4.7)	**7,155**	7,846	(8.8)	**7,510**	7,332	2.4
Switzerland	**5,999**	7,379	(18.7)	**1,917**	2,998	(36.1)	**5,406**	6,484	(16.6)
Luxembourg	**1,279**	989	29.3	**447**	453	(1.3)	**1,610**	2,010	(19.9)
Romania	**1,282**	1,280	0.2	**849**	860	(1.3)	**707**	680	4.0
Others abroad	**331**	608	(45.6)	**199**	454	(56.2)	**202**	480	(57.9)
Total	**374,360**	376,160	(0.5)	**240,874**	241,264	(0.2)	**286,003**	289,538	(1.2)

* Classified according to the location of the office.
For details regarding exposures to foreign countries, see the Management Review, Exhibit F of the Report.

The following table presents a breakdown of the net profit by geographical regions:

Region	Net profit NIS millions 2013	2012	Change %
Israel (1)	**1,993**	785	+
United States (2)	**66**	90	(26.7)
United Kingdom (3)	**(67)**	42	-
Switzerland (4)	**(57)**	(18)	-
Luxembourg	**15**	14	7.1
Romania (5)	**(7)**	8	-
Others abroad (6)	**4**	10	(60.0)
Total	**1,947**	931	109.1

The profit from activities abroad is shown according to their contribution in the consolidated financial statements.

(1) Net profit in Israel decreased by some NIS 1,208 million. Net profit after tax at the Bank in Israel increased due to the reasons set forth in the chapter, "Development of Income, Expenses and Tax Provision".
The net profit also increased at a number of subsidiaries in Israel, mainly: Leumi Partners and Leumi Card.

(2) The profits of the subsidiary in the United States fell compared with the corresponding period last year, as well as in terms of U.S. dollars, mainly as a result of an increase in expenses in respect of credit losses in 2013 compared with 2012.

(3) The profit of the subsidiary in the United Kingdom decreased relative to the corresponding period last year, as well as in local terms, mainly as a result of an increase in expenses in respect of credit losses in 2013 compared with 2012.

(4) The increase in the losses of the subsidiary in Switzerland derives from a one-time amortization of goodwill amounting to NIS 76 million provided in 2013.

(5) A loss in the overseas unit in Romania, compared with a profit in 2012, deriving from negative exchange rate differences in 2013.

(6) The profit relates mainly to Leumi Re, and the reduction derives from changes in insurance expenses.

For further details, see Note 27B to the Financial Statements.

Major Investee Companies*

The Leumi Group operates in Israel and abroad through subsidiaries which are: banks, finance companies and financial services companies. The Group also invests in non-banking corporations operating in the fields of insurance, energy, chemicals, infrastructure and real estate.

With regard to investments in non-banking corporations, see chapter, "Operating segments, Activity in Products and Profit Centers in the Group – Companies Included on Equity Basis (Non-banking)".

The Bank's total investments in subsidiaries and affiliates (including investments and capital notes) amounted to NIS 13,168 million on 31 December 2013, compared with NIS 13,513 million on 31 December 2012, and their contribution to the Group's net profit amounted to NIS 172 million, compared with NIS 601 million in 2012 (canceling the effect of Leumi Mortgage Bank, a decrease of NIS 126 million).

* For a definition of investee companies, see Note 1B to the financial statements.

The following table sets out the breakdown of the contribution of the Bank and its subsidiaries and investee companies to the net profit of the Group [(1)]:

	Return on Group's investment		Contribution [(1)] to Group's net profit		
	2013	2012	**2013**	2012	Change
	%	%	NIS millions		%
The Bank	**12.4**	3.2	**1,775**	330	+
Consolidated subsidiaries in Israel, total	**11.2**	7.5	**556**	562	(1.1)
of which: Leumi Mortgage Bank (2)	**-**	10.5	**-**	303	-
Arab Israel Bank	**21.7**	22.4	**106**	103	2.9
Leumi Card	**15.6**	15.9	**160**	144	11.1
Leumi Partners (3)	**40.6**	-	**213**	(68)	+
Leumi Capital Market Services Ltd.	**11.5**	14.2	**4**	4	-
Leumi Real Holdings	**1.2**	2.1	**11**	19	(42.1)
Leumi Finance	**7.7**	7.5	**13**	12	8.3
Leumi Tech (formerly, Leumi Leasing and Investments)	**2.2**	2.8	**22**	27	(18.5)
Others	**3.2**	2.4	**27**	18	50.0
Overseas consolidated subsidiaries, total	**-**	2.9	**(52)**	143	-
of which: Leumi USA (B.L.C.)	**2.6**	3.5	**66**	90	(26.7)
Leumi UK	**-**	5.3	**(67)**	42	-
Leumi Private Bank	**-**	-	**(57)**	(18)	-
Leumi Luxembourg	**6.2**	10.4	**10**	15	(33.3)
Leumi Romania	**-**	3.3	**(7)**	8	-
Leumi Re	**5.8**	11.4	**6**	10	(40.0)
Companies included on equity basis, total	**-**	-	**(332)**	(104)	-
Group's total net profit	**7.6**	3.8	**1,947**	931	109.1

(1) The profit (loss) shown is according to the company's share in the Group's results.
(2) Activity merged with the Bank on 31 December 2012.
(3) Including the profit and/or loss companies included on the equity basis of Leumi Partners.

See Note 6 to the Financial Statements concerning the investment in and contribution to Group profit of each of the major companies.

Consolidated companies in Israel

The Bank's total investments in consolidated subsidiaries in Israel amounted to NIS 5,295 million on 31 December 2013, compared with NIS 4,796 million on 31 December 2012. Their contribution to Group net operating profit amounted to some NIS 556 million in 2013, compared with NIS 562 million in 2012, a decrease of 1.1%. The decrease stems from the merger with Leumi Mortgage Bank at the end of 2012, and the inclusion of its profits as a part of the Bank's profits, which partially offset by an increase in the profits of Leumi Partners and Leumi Card. The Group's return on its investment in the consolidated companies in Israel was 11.2% in 2013 compared with 7.5% in 2012.

Financial and other data concerning the major consolidated subsidiaries are presented below on the basis of their financial statements:

The Arab Israel Bank Ltd.

The Arab Israel Bank was established in 1960 with the object of providing financial services to, and providing solutions for, the special requirements of the Arab population.

The Arab Israel Bank operates through two areas (North and South Galilee and the Northern Triangle) and 36 branches, situated mainly in the north of Israel and in the northern Triangle, serving the Arab population in these areas. Arab Israel Bank engages in the entire range of banking activities. The Arab Israel Bank's total assets amounted to NIS 6,868.9 million at the end of 2013, compared with NIS 6,103.9 million at the end of 2012. Net profit of the Arab Israel Bank totaled NIS 106.5 million in 2013, compared with NIS 103.1 million in 2012, an increase of 3.3%. The net return on shareholders' equity reached 21.2% as of 31 December 2013, compared with 21.8% at the end of 2012.

Shareholders' equity of the Arab Israel Bank amounted to NIS 553.0 million as at 31 December 2013, compared with NIS 526.8 million as at 31 December 2012.

The ratio of equity to risk assets as at 31 December 2013, reached 14.21%, as compared with 14.76% as at 31 December 2012. The Tier 1 capital (core capital) ratio to risk components at 31 December 2013 was 11.84%, compared with 10.84% at 31 December 2012.

The Arab Israel Bank receives comprehensive operating and financial services from the Bank. In consideration for the services received from the Bank, the Arab Israel Bank paid the Bank NIS 54 million in 2013, compared with NIS 46 million in 2012.

As a part of the implementation of the strategic work plan, the Bank has been operating on a number of levels to strengthen the bank in the Arab sector.

Within this framework, the Business Direct Center and Pension Consulting Center were established, in 2013, two new branches were opened and the existing branches were upgraded. In addition, the Bank launched a package exclusively for women, a MasterCard credit card and a portfolio management service.

In the area of customer experience, the Bank continued to upgrading activity in the digital channels, formulating value proposals adapted to customers' needs and assimilating the service.

Medium and Long-Term Financing Companies (1)

The assets of these companies amounted to NIS 20.0 billion at the end of 2013, compared to NIS 22.1billion in 2012. The business activity of these companies complements the activity of the Bank. The net profit of these companies amounted to some NIS 36.8 million in 2013, compared with NIS 41.9 million in 2012.

(1) Including: Leumi Industrial Development Ltd., Leumi Agricultural Development Ltd., Leumi Finance Company Ltd. and Leumi Tech (formerly, Leumi Leasing and Investments Ltd.).

The following are details concerning the main companies:

Leumi Tech Ltd (formerly Leumi Leasing & Investments Ltd.)

Leumi Tech will operate in future years to promote the activity of the Leumi Group in the area of banking services for the high-tech industry, including professional support for all of the Group companies in Israel and abroad, deepening ties with the industry, building and expanding the banking services and creating knowledge infrastructure – all this, in order to establish the Leumi Group as a key factor in the Israeli high-tech industry.

In the past, Leumi Leasing Ltd. financed the acquisition of equipment under leasing conditions for medium and long terms. In 2012, the Company ceased to finance new projects, but continued managing the existing leasing portfolio.
The balance of credit to the public totaled NIS 381 million as at 31 December 2013, compared with NIS 658 million at the end of 2012.

The company's total assets totaled NIS 1,035 million as at 31 December 2013, compared with NIS 1,049 million at the end of 2012.

The net profit in 2013 totaled NIS 22 million, compared with a profit of NIS 27 million in 2012.

Leumi Finance Company Ltd.

The company engages in the raising of financial sources in Israel for the Bank through issues to the public and private placements of securities, which do grant a participatory right in the company and are not convertible to shares – for example, debentures, subordinated notes, subordinated capital notes. The proceeds of these issues are deposited in the Bank for its use, at its discretion and its responsibility.

Total assets of the company amounted to NIS 19,063 million at the end of 2013, compared with NIS 20,851 million at the end of 2012. Shareholders' equity amounted to NIS 157.3 million as at 31 December 2013. The company's net profit amounted to NIS 12.6 million in 2013, compared to NIS 12.1 million in 2012.

The Bank has undertaken to indemnify Leumi Finance in respect of amounts that it is unable to pay, in respect of the indemnity that it granted to its directors and other officers and also to the lawyers of the said issues, with regard to these issues.

Leumi Partners Ltd.

Leumi Partners is the non-banking investments vehicle of the Leumi Group and specializes in providing a full range of investment banking services, business and financial services, capital raising and investments, mergers and acquisitions services, underwriting, organizing public and private issues, economic advice and appraisals. With regard to underwriting services, see paragraph C below.

Leumi Partners and its subsidiaries employ 35 employees, most of whom are economists, accountants or graduates in other subjects.

Leumi Partners finished 2013 with a profit of NIS 226 million, which arose mainly from the realization of investments and an increase in commission income, compared with a loss of NIS 43 million in 2012, which arose mainly from recording a provision for impairment amounting to NIS 160 million in respect of the investment in Partner Ltd.

Shareholders' equity as at 31 December 2013 totaled NIS 721 million, compared with NIS 473 million at the end of 2012.

Below are details concerning developments and main fields of activity:

A. Investments in non-banking companies

Leumi Partners is responsible for the management of the non-banking investment portfolio of the Leumi Group.

Leumi Partners engages in initiating, locating and carrying out direct investments in businesses and companies. Leumi Partners has invested in 50 companies, venture capital funds and private equity funds active in the fields of hi-tech, communications, commerce and real estate. The balance of the investments and undertakings to invest in these companies and businesses as at 31 December 2013 amounted to some NIS 461 million.

The non-banking investment policy of the Leumi Group is in line with the restrictions of the Banking (Licensing) Law, and therefore includes minority holdings (up to 20% of all means of control, and without control). The Group focuses on investments with the potential for long-term returns.

Leumi Partners invests in non-banking corporations as an auxiliary corporation under the provisions of the Banking (Licensing) Law.

Since it is unable to control the companies in which it has invested in the light of the law's restrictions, Leumi Partners stringently examines the quality of the management, the strength of the partners and the nature of the investment.

B. Investment banking services

Leumi Partners assists its customers in executing merger and acquisition (M&A) transactions. The services are provided to Israeli and foreign companies wishing to effect strategic expansion by way of acquisition, or to investors or controlling shareholders interested in selling or reducing their investments.

The basket of services within this framework includes: assistance in the definition of the company's requirements and strategic objectives, the determination of the optimal investment/investor for the achievement of those objectives, the identification of target investments/investors on a global basis, assistance in making contact with the target company, involvement in negotiations until their conclusion (deal structuring), in a manner that serves the customer's objectives and assistance in accessing sources of finance for the transaction.

In its operations, Leumi Partners cooperates with investment houses and other entities in Israel and around the world.

C. Underwriting and management of issues

The subsidiary company Leumi Partners Underwriting Ltd. engages in the management and underwriting of private and public issues of securities in the capital market in Israel.

In 2013, Leumi Partners Underwriting was one of the leading underwriters in the Israel market. Leumi Partners Underwriting participated in public issues for a total amount of some NIS 16.5 billion, and led 31 public issues for a total of some NIS 5.6 billion.

D. Economic analyses and appraisals

The subsidiary Leumi Partners Research engages in economic analyses, economic appraisals and financial counseling, mainly for the Leumi Group and economic entities in the Israeli economy.

The company prepares economic studies and valuations for the purposes of investments, mergers and acquisitions, making loans and debt evaluation.

In addition, the company reviews the large companies traded on the Israeli capital market, as well as a number of Israeli companies traded abroad and bonds traded on the Israeli capital market and for institutional entities.

The Bank Leumi le-Israel Trust Co. Ltd.

This company, founded in 1939, provides a range of trust services which address the business and personal needs of its customers. In the capital market field, the company serves as trustee of liability notes, including exchange traded certificates, and also as a trustee of pledged shares. Other fields of activity in which the company engages: management of real estate assets (including buying and selling), escrow accounts – supervision of agreement implementation, managing private and public funds, executing wills and administering collateral trust estates and representation at general meetings of companies for foreign banks.

The company's income from trust business for 2013 amounted to NIS 11.8 million compared with NIS 11.9 million in 2012. The company's net profit in 2013 amounted to NIS 3.3 million, compared with NIS 3.9 million in 2012.

For information on the legal claims against the trust company, see note 18 in the financial statements**.**

Competition

The company's main competitors are trustee companies of large accounting/law firms, some of the banking trustee companies and other entities providing trust services.

Customers

The company provides services to a range of customers; to private customers, management of private and public funds, financial asset management, real-estate management and the execution of wills and the management of estates, to business customers, companies and institutional bodies it provides trust services for issues of liability notes and ETF certificates, pledges on shares, trustee of securities and representation at general meetings of companies of foreign banks.

Trust Business

In addition to the Bank Leumi le-Israel Trust Co. Ltd. mentioned above, a number of additional companies in the Group also engage in trust services, a subsidiary of Bank Leumi UK in the Island of Jersey and Bank Leumi USA.

The trust activities in the Group yielded the following income:

- Trusteeship for monies, securities and real estate, some NIS 13.6 million (NIS 13.6 million in 2012)
- Estate and property management , some NIS 0.5 million (NIS 0.6 million in 2012).
- Agent for deposits and loans, share transfers, and management of investment accounts, some NIS 2.6 million (NIS 6.8 million in 2012).
- Trustee for debenture and mutual fund holders, some NIS 4.3 million (NIS 3.8 million in 2012)

Overseas Consolidated Companies, Branches and Agencies

The Group's international activity is carried out by a network of investee companies, branches, agencies and representative offices spread across 15 countries in 52 offices and branches. The Bank's main subsidiaries are located in the world's most important financial centers: New York, London, Zurich and Luxembourg.

The Group’s deployment overseas is operated in order to maximize the business potential of Israeli corporate customers, local middle-market customers operating in sectors of the economy in which Leumi has the expertise, know-how and resources needed to provide financial services, international entities operating in Israel and the local Jewish communities in the places where the units are located. The Bank’s major overseas target population is commercial companies and wealthy private customers. These customers receive a range of services from the units, such as private banking services, investment financing, foreign trade and transactions in foreign currency and their derivatives. The cooperation between the overseas units and the Bank in Israel and amongst the overseas units enables maximum utilization of the relative advantage of each and every unit. In late 2012, organizational changes were made in the format of international activity in the Group with the aim of strengthening the control, supervision and review of the Bank's overseas units. The main organizational changes include:

- The appointment of a member of management or head of a division as the official responsible for a unit, which is in charge of to the unit's day-today business direction and the management of the interaction between the units and Leumi management, with the aim of enabling the allocation of administrative resources at the highest level and strengthening the link with Group management, to participate in crystallizing the business policies and setting out the unit's strategy. Responsible officials were also appointed to the boards of directors of the units.

- The establishment of an international activity staff in the Finance and Economics Division. The staff is responsible for the Group's monitoring and control of international activity, an information center, processes and broad areas in all matters related to international activity *vis-à-vis* the official responsible for the units, Bank management, the Board of Directors and Bank of Israel and represents a supporting factor in receiving the assistance required from Tel Aviv.

- The reinforcement of the professional support in the international activity by the units of expertise, i.e., the professional divisions, e.g., risk management, human resources, operations and IT, audit, accounting, etc. These units represent a central address for supporting the units on professional subjects, and accordingly, have professional responsibility over the areas of activity required for the management of the international activity in their area of expertise. The professional authority of the units of expertise will include, *inter alia*, a delineation of collective policy, professional regulation, periodic reports to Leumi management, to head office and the officer in charge of the units.

Quarterly reports on ongoing developments and special findings in the units are sent to the management every quarter and to the Board of Directors every six months.

The Risk Management Division carries out routine monitoring, analysis, identification, mapping and evaluation of material focuses of risk in the overseas units.

In September 2013, the requisite approvals were received from the regulatory authorities in China to establish a representative office of the Leumi Group in Shanghai. The establishment of the representative office is the fruit of a strategic initiative of Leumi to penetrate new markets and open them to the Group's business. The representative office constitutes the first time an Israeli bank has made its way into China. By virtue of a license held by the representative office, its area of operations is limited to activity of a marketing nature only, including the gathering of information on the market, the establishment of a potential customer base and the examination of the feasibility of future activity in China. The representative office is subject to the Head of the Capital Markets and Private Banking and Strategy Division.

At the end of 2013, a decision was taken to close the representative offices in France, Chile and Toronto. At the end of 2013 and the beginning of 2014, the representative offices in Australia and Hong Kong were closed. The Bank is taking steps to close its representative offices and return the licenses to the regulatory authorities in the relevant countries. The Group will adapt the nature of its activity and deployment in accordance with changes in international (off-shore) private banking.

In February 2014, the central bank of Argentina announced the adoption of administrative proceedings against two former representatives of the Bank in Argentina, in respect of the failure to provide information it requested relating to transactions entered into in the past via the Bank, by Argentinean resident customers, in the period from April to June 2010. It should be noted that Bank's representative office in Argentina ceased to operate in October 2011.

German authorities are conducting investigations into the customers of the Leumi Private Bank AG in connection with the failure to report to the tax authorities, and within this context, they have issued subpoenas relating to customers and a representative of the Bank in Germany.

The Bank's total investment in overseas units at the end of 2013 amounted to NIS 4,597 million, compared with NIS 4,940 million at the end of 2012.

The following table sets forth the contributions of the major overseas consolidated companies to the Group's net profit:

	Yield on the Group's investment for the year ended 31 December		Contribution to the Group's profit for the year ended 31 December		
	2013	2012	**2013**	2012	Rate of change
	%		NIS millions		%
Leumi USA (B.L.C.)	**2.6**	3.5	**66**	90	(26.7)
Leumi UK	**-**	5.3	**(67)**	42	-
Leumi Private Bank	**-**	-	**(57)**	(18)	-
Leumi Luxembourg	**6.2**	10.4	**10**	15	(33.3)
Leumi Re	**5.8**	11.4	**6**	10	(40.0)
Leumi Romania	**-**	3.3	**(7)**	8	-
Others	**-**	-	**(3)**	(4)	+
Total of overseas consolidated companies	**-**	2.9	**(52)**	143	-

With regard to the treatment of translation adjustments in respect of foreign investments since 1 January 2012, see note 1E.

.

The following table sets forth details of the net profit (loss) of the overseas units, as reported by them:

	2013	2012	Change
	In millions		%
Leumi US (BLC) - US$	**11.4**	22.5	(49.3)
Of which: Bank Leumi USA - US$	**11.0**	22.5	(51.1)
Bank Leumi UK - £	**(5.4)**	4.6	-
Leumi Private Bank - CHF	**7.5**	0.2	+
Bank Leumi Luxembourg - euro	**2.9**	3.0	(3.3)
Leumi Romania – ron *	**2.1**	13.6	-
Leumi Re - US$	**3.3**	4.6	(28.3)
Others - US$	**-**	(0.7)	-
Overseas branches -US$	**1.5**	2.0	(75.0)
Total in dollar terms	**20.4**	44.1	(53.7)

* 1 Ron = NIS 1.0659

The following table sets forth a summary of the assets and liabilities of the Bank's overseas units and branches (in US$ millions* prior to offsetting mutual balances):

	31 December	
	2013	2012
Credit to the public	**6,769**	7,125
Deposits with banks	**2,843**	3,124
Securities	**1,312**	1,379
Other assets	**369**	385
Total	**11,293**	12,013
Deposits of the public	**8,507**	8,939
Deposits from banks	**829**	1,114
Other liabilities	**581**	578
Shareholders' equity	**1,376**	1,382
Total	**11,293**	12,013
Total trust deposits and securities under management	**11,374**	11,305

The total balance sheet of the consolidated overseas subsidiaries and branches of the Bank amounted to US$ 11.3 billion (NIS 39.2 billion) at the end of 2013, compared with US$ 12.0 billion (NIS 44.8 billion) at the end of 2012.

* The translation to US$ is a convenience translation of the data according to the representative rates of exchange on 31 December 2013 and 31 December 2012, respectively.
The amounts are as published by the overseas units.
The data in shekel terms is presented in the report according to sectors - see Note 27 to the Financial Statements.

The following table sets out principal data regarding the Bank's overseas units (in US$ millions) at 31 December 2013:

	USA	UK	Switzerland	Luxembourg	Romania
Total assets	**5,191**	**2,670**	**1,921**	**729**	**368**
Credit to the public	**3,678**	**2,058**	**552**	**128**	**245**
Deposits of the public	**4,422**	**2,195**	**1,579**	**430**	**204**
Shareholders' equity	**547**	**213**	**271**	**59**	**70**
Trust deposits and managed securities	**4,143**	**408**	**5,583**	**944**	**-**
Net profit	**11**	**(8)**	**8**	**4**	**1**
Return on equity (%)	**2.3%**	**-**	**3.2%**	**8.4%**	**0.9%**

The net profit for all the consolidated overseas companies, including overseas branches, as published by them, totaled US$ 29.2 million in 2013, compared with a profit of US$ 42.1 million in 2012, a decrease of US$ 12.9 million.

The negative contribution of the overseas units to the net profit of the Group in shekels in 2013 amounted to a loss of NIS 52 million, compared with a profit of NIS 143 million in 2012.

See Notes 6 and 27 to the Financial Statements for further details concerning the contribution of the units to the Group's profit.

Bank Leumi le-Israel Corporation

Bank Leumi le-Israel Corporation ("BLL Corp.") was incorporated in the United States in 1984 and is a wholly owned subsidiary of the Bank. BLL Corp. is defined under US law as a bank holding company, and its principal activity is the holding of its subsidiary, Bank Leumi USA.

BLL Corp.'s total assets amounted to US$ 5.2 billion as at 31 December 2013, compared with US$ 5.4 billion at the end of 2012, and the annual profit amounted to US$ 11.4 million, compared with US$ 22.5 million in 2012, a decrease of 49%.

The decrease in net profit resulted primarily from an increase in expenses in respect of credit losses, a decrease in operating income and an increase in operating expenses. The return on equity of BLL Corp. reached 2.3% compared with 3.35% in 2012.

As at 31 December 2013, the equity amounted to US$ 692 million. The ratio of equity to total assets was 13% and the ratio of equity to risk assets was 16%.

Bank Leumi USA

Bank Leumi USA (BLUSA), incorporated in 1968, holds a commercial banking license from the State of New York and is a member of the FDIC (Federal Deposit Insurance Corp.).

BLUSA engages in commercial banking, primarily financing medium and larger sized (middle-market) local companies, in international banking, mainly with Israeli companies, and also private banking for U.S. and non-U.S. residents. BLUSA offers full banking services to Israeli companies and to Israeli residents interested in the products and services of an American bank.

BLUSA's consolidated assets amounted to US$ 5.2 billion on 31 December 2013, compared with US$ 5.4 billion at the end of December 2012. Total shareholders' equity amounted to US$ 547 million on 31 December 2013 compared with US$ 541 million at the end of 2012. Credit to the public totaled US$ 3,677 million at the end of 2013, a decrease of 0.8%, while deposits of the public, which totaled US$ 4,422 million, decreased by 2.7%.

Customers' managed securities portfolios, which are not included in the balance sheet, totaled US$ 4,132 million at the end of 2013, compared with US$ 3,935 million at the end of 2012.

BLUSA ended 2013 with a net profit of US$ 11 million, compared with US$ 22.5 million in 2012.

The return on equity of net profit in 2013 was 2.54% compared with 4.78% in 2012.

The balance of the expenses in respect of credit losses at the end of 2013 amounted to US$ 10.8 million, constituting 0.3% of total credit to the public.

The ratio of equity to total assets is 10.5% (10.1% in 2012) and the ratio of equity to risk assets was 14.54% (14.47% in 2012). These ratios exceed the US supervisory authorities' requirements and transition to the Group's capital adequacy requirements.

On 1 September 2013, Mr. Avner Mendelson, Head of the Strategy Department and International Operations Headquarters was appointed to the position of General Manager of BLUSA in place of Mr. Yitzhak Eyal, who ceased to serve in his position and will retire from Bank Leumi in June 2014.

Towards the end of 2012, BLUSA began implementing a strategic program ("Running for 10") including a number of initiatives intended to improve the bank's long-term profitability increasing business focus, upgrading core abilities and systems and operational streamlining. As a part of this program, in the fourth quarter of 2012, BLUSA began implementing a process of merging branches for streamlining and cost savings, maintaining a presence in four countries. As of the end of 2013, BLUSA had seven branches. At the end of 2013, the BLUSA branch in the Cayman Islands was closed.

In addition, within this framework, BLUSA entered into agreements in connection with the sale of its interests in two buildings in New York. The execution of the agreements is contingent on complex commercial conditions. If all of the conditions are fulfilled according to the assessment of BLUSA's management, the sale is likely to take effect by the end of 2015. In view of the uncertainty, it is not possible, at this stage, to give a reliable estimate of the expected gain on the sale, if any.

At the end of 2013, BLUSA commenced a project to replace the core system through the supplier of the current core system.

During 2013, a business initiative was formulated with the broad purpose of trade activity in Leumi Investments Services Inc. (LISI), which will improve the value proposition to BLUSA customers.

In July 2012, Mr. D. Brodet, Chairman of the Board of Directors of Leumi Group, was appointed chairman of the board of directors of Bank Leumi USA, in place of Mr. S. Levine, who is continuing to serve as a member of the board of directors.

The Bank's Branches and Agencies

The Bank operates an agency in New York, a branch in Panama and a branch in Georgetown.

Total assets of the agency in New York and the branches in Panama and Georgetown amounted to some US$ 144 million at the end of 2013 (before offsetting mutual balances), compared with some US$ 705 million at the end of 2012. Credit to the public totaled US$ 37 million at the end of 2013, compared to US$ 114 million at the end of 2012. Deposits of the public totaled US$ 32 million at the end of 2013, compared with US$ 104 million at the end of 2012. 2013 ended with a profit of some US$ 2 million, compared to US$ 27 million in 2012.

The Board of Directors of Leumi took a decision to close the Panama branch through its liquidation. The process was managed by the Panama branch manager.

The Georgetown branch is registered in the Cayman Islands and operates in accordance with the local laws and directives. Due to the increase in the operational costs of the branch in recent years, the Bank has taken active steps to reduce the number of customers in the branch.

Bank Leumi UK

Bank Leumi UK plc was founded in 1959 and continues the activity of the Group in England that began in 1902. It is currently the largest Israeli-owned bank in the United Kingdom. The bank's center of activity is in London and, in addition, the bank has two subsidiaries – a banking subsidiary on the Island of Jersey, Bank Leumi (Jersey) Ltd. and also a trust company in Jersey, Leumi Overseas Trust Corporation Limited, which is wholly-owned by Bank Leumi Jersey, and Leumi ABL Ltd., a subsidiary engaged in the area of asset-based lending, operating in the field of discounting and factoring of invoices.

Bank Leumi UK is engaged in commercial and private banking. The commercial banking activity includes real estate financing, international trade, finance of media, mainly in Europe, Israel-related business and Israeli companies active in the UK.

Bank Leumi UK finances a wide range of activities in the real estate field in the UK and Western Europe, including investments and development of residential real estate and the financing of commercial real estate (mainly hotels, retirement homes, and student halls of residence). The financing is provided to both local and non-resident customers (mostly Israelis).

Bank Leumi UK ended the year 2013 with a loss of £ 5.4 million, compared with a profit of £ 4.6 million in 2012. The loss resulted from an increase in expenses in respect of credit losses mainly in respect of real estate credit or to holding companies focused on this area. Subsidiaries of Bank Leumi UK ended 2013 in profit.

Total consolidated assets of Bank Leumi UK amounted to £ 1,614 million at the end of 2013, similar to the end of 2012.

Deposits of the public increased from £ 1,235 million at the end of 2012 to £ 1,327 million at the end of 2013. Bank Leumi Jersey's portion of the balance of deposits at the end of 2013 was £ 333 million. Credit to the public decreased from some £ 1,298 million at the end of 2012 to £ 1,244 million at the end of 2013. Bank Leumi Jersey's portion of the balance of credit at the end of 2013 was £ 125 million.

Capital, reserves and surpluses totaled some £ 129 million at 31 December 2013, compared with some £ 134 million at the end of 2012.

On 22 February 2013, Bank Leumi Jersey paid a dividend amounting to £ 4 million to Bank Leumi UK.

In 2013, there was a change in the regulatory authorities in the United Kingdom. The Financial Services Authority (FSA) was replaced by two regulatory authorities: the Financial Conduct Authority and the Prudential Regulation Authority. The two bodies are responsible for the regulations applicable to financial institutions. As a result, there may be changes in the regulations applicable to banks.

The ratio of equity to assets amounted to 8.0% (8.3% in 2012)

Leumi Private Bank S.A. (formerly Bank Leumi Switzerland)

Bank Leumi (Switzerland) (above and below "Bank Leumi Switzerland"), was founded in 1953.

On 10 February 2011, an agreement (hereinafter: "the purchase agreement") was signed between Bank Leumi Le-Israel Ltd. (hereinafter: "Leumi"), directly or through a company under its control, and Island Tower Foundation, Helena S. Safdié Levy, Edmundo Safdié, and G.RS. Participations S.à.r.l., the owners of Banque Safdié SA in Switzerland (hereinafter: "Banque Safdié"), according to which Leumi will purchase all of the share capital in the acquired bank,

According to the purchase agreement, the basic consideration amount, before adjustments, will be based on the net asset value of the acquired bank, with the addition of a premium on the assets under management of the acquired bank on the date of the transaction's closing, and it will be adjusted in accordance with the results of a due diligence examination.

On 30 November 2011, after the preconditions set forth in the agreement were fulfilled, the purchase agreement was completed and Leumi purchased the entire share capital of Banque Safdié. Pursuant to the purchase agreement, the total consideration paid at the closing date of the transaction was CHF 143 million, of which CHF 110 million was paid to the sellers and the balance of CHF 33 million deposited on trust (hereinafter: "the trust account") to secure adjustments in the consideration derived from changes in the assets managed by Banque Safdié in the 24 months following the date of completing the transaction, and other adjustments in accordance with the formulas agreed between the parties. The trust account was also intended to secure the liabilities of the sellers for indemnities set forth in the purchase agreement.

On 3 January 2012, the merger with Banque Safdié was formally completed and pursuant thereto, the activity of Banque Safdié was merged with that of Bank Leumi Switzerland. In April 2012, the merger of the automated systems was completed. The name of the merged bank was changed to Leumi Private Bank SA (LPB), as approved by the general meeting of the shareholders of the Bank Leumi shares when they convened on 19 December 2011.

On 5 October 2012, an adjustment was made to the purchase price, according to the net asset value and the assets managed by Banque Safdié, as they were on the purchase date. Accordingly, on 11 October 2012, a further payment of CHF 484 thousand was transferred directly to the sellers.

On 17 October 2012, the enlargement of the share of the minority shareholder to 5.03% of the share capital of LPB was completed. The Bank issued 2,840 new Class B shares at a price of CHF 1,777.25 per share and received aggregate consideration of CHF 5,048,100.

The sellers and Leumi have yet to reach an agreement regarding the amount of the price adjustment. Only when agreement is reached on the subject, will monies be released from the trust account.

On 20 February 2013, the board of directors of Leumi Private Bank resolved to close the subsidiary, MBCO, in the Cayman Islands. At the end of November 2013, the authorities in the Cayman Islands gave their approval for the return of the license and the liquidation of the company. In the financial statements of LPB (company only), a loss in respect of the investment in the company amounting to CHF 482 thousand is recorded.

Total assets of Leumi Private Bank amounted to CHF 1,705 million at the end of 2013, compared with CHF 1,902 million at the end of 2012. 2012 was a year of synergy of the two banks that merged. Profit in 2013 amounted to CHF 7.31 million, compared to a total of CHF 0.3 million in 2012.

The total of capital and reserves, including internal funds, amounted to CHF 241 million at the end of 2013, compared with CHF 237 million at the end of 2012.

Total assets managed and/or held for customers and not included in the balance sheet at the end of 2013 amounted to CHF 5.6 billion, compared to CHF 5.2 billion at the end of 2012.

In light of the change in regulations in the area of international private banking around the world, and in Switzerland, in particular, which has increased the cost of the service, and in light of the expected impact of these changes on Leumi Private Bank (formerly Bank Leumi Switzerland) as well, in 2013, the Bank amortized NIS 79 million from the goodwill.

In February 2014, Professor Daniel Tsiddon was appointed chairman of the board of directors of Leumi Private Bank, replacing Ms. Galia Maor, who submitted her resignation from the board of directors.

Bank Leumi Luxembourg

Bank Leumi Luxembourg was established in 1994 and opened to the public in May 1995. Bank Leumi Luxembourg provides its customers with a variety of private banking services, including deposits and investments in securities.

Total assets at the end of 2013 amounted to some € 530 million, compared with some € 473 million at the end of 2012.

At the end of 2013, deposits of the public totaled some € 312 million compared with some € 397 million at the end of 2012. Customers' assets held by customers of the bank and not included in the balance sheet totaled € 685 million at the end of 2013, compared with € 739 million in 2012.

Bank Leumi Luxembourg ended 2013 with a profit of € 2.9 million, compared with a loss of € 3.0 million in 2012.

The capital means of Bank Leumi Luxembourg totaled some € 43 million, compared with € 40 million at the end of 2012.

The infrastructure system in Leumi Luxembourg has been replaced. The system was up and running in July 2013.

In March 2013, Professor Daniel Tsiddon was appointed chairman of the board of directors of Leumi Luxembourg.

Leumi International Investments N.V. ("L.I.I.")

The purpose of the company in the past was to serve as a vehicle to issue notes of the Bank Leumi Group to the public overseas. The company was closed in August 2013.

Bank Leumi Romania

In August 2006, the Bank acquired over 99% of the issued and paid-up share capital of Eurom Bank S.A. from S.C. Kolal B.V. The name of the company was changed to Bank Leumi Romania in August 2006.

Leumi Romania is a banking corporation in Romania, and operates 21 branches, and engages in financial activity that includes, *inter alia*, the accepting of deposits, the extension of credit, international trade and foreign currency activities.

The commercial banking activity includes real estate financing, the financing of Israeli customers operating in Romania and the financing of small and medium-sized local businesses.

In view of the economic situation in Romania and following an examination of the future potential of activity, in 2013, the bank shut two branches following a contraction of 13 branches in 2010-2012.

Leumi Romania ended 2013 with a profit of 2.1 million Romanian ron (some US$ 0.6 million), compared with a profit in 2012 of some 13.6 million Romanian ron (some US$ 3.9 million). The fall in profit arises mainly from an increase in expenses in respect of credit losses.

Following the negative growth rate of the Romanian economy in 2009-2010, due to the harshest recession for 20 years, there was a moderate improvement in the country's economy since 2011. The growth rate is expected to increase gradually as a result of the increase in the amount of investments in support grants from the European Union, which will be received under a number of conditions, including reforms in the government authorities and an increase in competition in sectors controlled by government companies.

The assistance program of the International Monetary Fund to Romania (Standby Arrangement) was approved in 2013 for a further two years.

The banking system in Romania is still vulnerable to external shocks, particularly due to the high proportion of foreign banks, mostly Austrian and Greek. The capital adequacy ratio of the banks is good, although loans, classified as problematic, are on a rising trend, and the level of credit activity continues to moderate.

The total assets of Bank Leumi Romania amounted to 1,198 million Romanian ron (US$ 368 million) at the end of 2013, compared with 1,150 million Romanian ron (some US$ 342 million) at the end of 2012. Deposits of the public amounted to 665 million Romanian ron (some US$ 204 million) at the end of 2013, compared with some 614 million Romanian ron (some US$ 182 million) at the end of 2012, and credit to the public amounted to 797 million Romanian ron (some US$ 245 million), compared with some 775 million Romanian ron (some US$ 231 million) at the end of 2012.
The capital, reserves and surplus amounted to some 227 million Romanian ron (some US$ 70 million) at the end of 2013, compared with 224 million Romanian ron (some US$ 66 million) at the end of 2012.

1 Romanian ron = US$ 0.307 (31 December 2012- US$ 0.297)

On 6 March 2013, Mr. Yoel Mintz, Head of the International Credit and Real Estate Division, was appointed as chairman of the board of directors of Bank Leumi Romania, in place of Mr. Zvi Itskovitch, who retired from his post due to his retirement from the Bank.

Leumi (Latin America)

Leumi (Latin America) S.A. was established in 1980 and operates through a head office in Montevideo and a branch in Punta del Este. Leumi (Latin America) provides general banking services.

Total assets of Leumi (Latin America) were US$ 47 million at the end of 2013, similar to the end of 2012.

Capital, reserves and retained earnings totaled some US$ 10 million on 31 December 2013, compared with US$ 11 million in 2012.

2013 ended with a profit of some US$ 137 thousand compared with a loss of some US$ 398 thousand in 2012. The balance of off-balance sheet activity totaled some US$ 297 million in 2013, compared with US$ 301 million at the end of 2012.

In January 2013, a court in Brazil handed down a verdict of public service and fines against two people who had acted as representatives of the bank in Porto Alegra, with regard to events connected to the transfer of monies via moneychangers during 2003-2004.

Leumi Re Ltd.

In June 2002, the Bank established Leumi Re Ltd. in the Island of Guernsey. The company is wholly owned by the Bank and serves as a reinsurer for insurance companies that insure the Leumi Group. The company's issued capital is US$ 30 million, of which US$ 6 million is fully paid. Furthermore, the Bank undertook in a guarantee to make additional amounts available to Leumi Re Ltd., up to an amount of US$ 9 million.

The Bank has also given an unlimited guarantee to the insurer, New Hampshire Insurance Company, to secure payment of the insurer's claims with respect to Leumi Re Ltd.

The company was established with the approval of the Bank of Israel, which determined that:

- The Bank shall hold 100% of the means of control of the company.
- The company shall engage in banking insurance, liability insurance and property insurance,
- The company shall only engage in insurance for the Bank Leumi Group.

The company's **total assets** at the end of 2013 amounted to US$ 38.4 million, compared with US$ 38.3 million at the end of 2012, and the **insurance reserves** amounted to some US$ 19.2 million at the end of 2013, compared with some US$ 18.5 million at the end of 2012.
Shareholders' equity amounted to some US$ 12.9 million as of 31 December 2013, compared with US$ 14.5 million at 31 December 2012
Profit for 2013 amounted to US$ 3.3 million, compared with a profit of US$ 4.6 million in 2012.

Since 2003, the financial statements of the company have been prepared on the basis of the revised accounting rules of the Association of British Insurers. In accordance with these rules, the company's financial statements are prepared on an annual basis, according to which the insurance reserves are calculated on the basis of an assessment of the estimated cost of settling the claims that have been reported, as at the date of the statements.

Activities of Companies Included on Equity Basis

Total investments of the Group in companies included on equity basis amounted to NIS 1,689 million as at 31 December 2013, compared with NIS 2,129 million as at 31 December 2012. The negative contribution to net operating profit of the companies included on the equity basis amounted to a loss of NIS 293 million in 2013, compared with a loss of NIS 67 million in 2012.

For further details, see above in the chapter, "Operating Segments, Product Activities and Profit Centers in the Group – Companies Included on Equity Basis".

Exposure to Risk and Methods of Risk Management

Risk management

Risk management in Leumi

The Bank is engaged in a wide spectrum of financial activities that involve the taking of risks, primarily credit risks and market and liquidity risks. These risks are accompanied by operational risks and compliance risks inherent in business activity. Risk management in Leumi is considered an essential condition for fulfilling the Group's long-term goals. The main goal of risk management in Leumi is maintaining the stability of the Bank and the Group, and complying with the risk appetite established by the Board of Directors. This includes minimizing material losses and events that may significantly impair the Bank's reputation. In addition, the goal of risk management is to support the achievement of business goals, with continued activity to upgrade the risk management infrastructure and analysis of the risk picture, enabling more educated decision-making and expansion of activity.

Risk management framework

Risk management in Leumi is led by the Chief Risk Officer, who is a member of management in the Bank, and Head of the Risk Management Division. The Chief Risk Officer is responsible for managing the main risks in the Bank and in the Group, with the management of legal risk under the authority of the Bank's Chief Legal Advisor and the management of goodwill risk under the responsibility of the Head of the Marketing, Advertising and Spokesperson's Department. In the risk management structure which has been established, the Risk Management Division is an independent entity which places emphasis on overall supervision and is involved in making material decisions in real-time. Reporting to the Chief Risk Officer are the heads of the departments for managing credit risks, market risks, operating risks, an overall risk-return manager and the Head of the Compliance Department. With effect from the beginning of 2014, the credit risk management (CRM) units, which independently analyze credit risks above NIS 25 million were made subject to the Chief Risk Officer. At the same time, overall responsibility for the appropriateness of classifications and allowances in the Bank was transferred to the Risk Management Division. These changes are in accordance with Proper Conduct of Banking Business Directive no. 311 which was published in December 2012. In the said procedure, the Banking Supervision Department requires a higher involvement at the transaction level of the risk management function that what has been required to date. The regulation provides that the risk management function is obliged to express its opinion individually on credit transactions of amounts in excess of NIS 25 million and that the decision regarding classifications and allowances should be carried out by a party that is independent of the business party.

Risk management in Leumi is based on three "lines of defense". The first line of defense is the corporate divisions, which are responsible for taking, analyzing and understanding risk throughout the life of the transaction and activity; the second line of defense is the Risk Management Division, which is responsible for leading policy and risk limitation, in conjunction with the business party and the directives of the Board of Directors, and the challenge of the corporate divisions in important decisions; and the third line of defense is the Internal Audit Division, which retrospectively monitors the first two lines of defense. In addition to these three lines of defense, the Board of Directors is involved in the determining, supervising and contesting the risk levels to which the Bank and the Group are exposed.

The main areas of responsibility of the Risk Management Division correspond to those defined in Proper Conduct of Banking Management Regulation no. 310 dealing with risk management, published in December 2012. These include directing Leumi's risk policy with regard to all of the main risks, assisting the Board of Directors in crystallizing the Bank's risk appetite, making independent analyses when strategic decisions are reached and in the approval procedures for approving new products, and form an overall and up-to-date picture of the risk for making real-time decisions.

Control and inspection of risk management are conducted by the management committees for the management of the various risks, as well as the Risk Management Committee of the Board of Directors, as set forth below:

- The Risk Management Committee of the Board of Directors
- The Upper Risk Management Committee headed by the President and CEO, of which all of the members of the management are members.
- Risk management committees according to various topics headed by the Chief Risk Officer and with the participation of factors from the various divisions: credit, market, operational and overall risk.

The committees outlined above discuss aspects of exposures to the various risks and determine internal restrictions in accordance with the conditions of the market and the Bank's risk appetite.

Risk management in the subsidiaries is conducted in accordance with the principles prescribed at the Group level. A chief risk officer is appointed in each subsidiary in Israel and abroad, and there are policy documents relating to the management of the principal types of risk, derived from the Group policy in each of the risk areas. Risk appetite, limits and authorities are determined, and there are also control systems and periodic management reports examining the limits against the actual position. The risk managers in the subsidiaries report to the CEO of the subsidiary and, on a professional level, to the Chief Risk Officer of the Group.

Main risks

The main risk of the Group is credit risk, which includes credit to the public, banks, governments, securities, derivatives and the like. This risk is in accordance with the core business of the Group and is reflected in activity with corporate, commercial and retail customers, as well as *nostro* activity. The Bank's policy in Israel is to take steps towards a maximum dispersal of risk. The Bank aims to ensure that management of the credit portfolio, the determination of the level of working facilities with borrowers, limitations on the credit portfolio and the measurement of concentrations are in terms of risk and return on risk indices and not just in terms of exposure. The allocation of dealing with customers among lines of business is carried out according to the level of indebtedness and the level of complexity/specialization of the type of transaction, in order to ensure the required level of expertise for dealing with each sector and type of activity.

(For details of credit risk and its management, see below in this chapter.)

Market risk, including liquidity risk, is the second most important risk. The routine management of market risks is intended to support the achievement of business targets, while estimating the forecast profit against the damage likely to emanate from exposure to these risks. Exposures to market risk are managed dynamically. The system of limitations determined by the Board of Directors and the risk committees at different levels delineates the impact of exposure on the economic value, the accounting profit, capital reserve and liquidity position. (For details of market risk and its management, see below in this chapter.).

(For details of market risk and its management, see below in this chapter.)

In recent years, as a result of innovativeness in legislation and the principles of enforcement, compliance with the fabric of the international laws and rules has become far more complex than in the past. In addition, tolerance of enforcement factors to partial compliance has fallen. Accordingly, the risk originating in partial compliance has increased greatly, whether it comes from an error, lack of information or from belated assimilation. In particular, in addition to consumer subjects and issues of money laundering and the financing of terrorism, in the fabric of the laws and regulations to which the Bank is required, the weight of issues connected to the investment management rules of customers in other countries (cross-border), and the share of the issues connected to the compliance of customers to the tax laws relevant to them has increased. This risk management is carried out through the Compliance Department which is subject to the Chief Risk Management. This risk is called hereinafter "compliance risk" and is, by virtue of its definition, the risk which exists from failure to comply fully and timely with various regulations. In recent years, many banks around the world have absorbed substantial penalties in respect of the exposure to this risk. Compliance risk management is effected through the Compliance Department, which is subject to the Chief Risk Officer.

In the Bank's activity as a financial intermediary, there are operational risks which also include, inter alia, the areas of business continuity and information security. Operational risk management is conducted in accordance with the generally accepted (best practice) standards in all parts of the Group.

(For details of operational risk and its management, see below in this chapter.)

Tools used in managing risk

The methods and procedures for working in the area of risk management in Israel and abroad are examined and revised on an ongoing basis, taking into account the policy of the Bank, changes occurring in the business environment, and the directives and requirements of the Bank of Israel, as well as other relevant regulatory authorities in Israel and abroad. Set forth below is a condensed review of the principal tools used for estimating the risks and as a basis for decision-making. The main tools used in the management of risk are: the determination of the risk appetite, which defines, inter alia, the establishment of risk policies and restrictions - for each type of risk; the setting of work processes for analyzing and managing risk at the single transaction level and at portfolio level; periodic reports for evaluating risk on the basis of qualitative and quantitative indicators of Leumi's portfolio, taking account of changes in the environment in which the Bank operates. These reports are discussed in forums and various committees defined for the subject; conducting various potential scenarios, at various levels of severity, for assessing the potential losses and implications for the Bank. On the basis of these scenarios, conducted at both Bank level, and at the level of the specific type of activity and risk, a plan of action to be carried out to contend with the risks is defined.

The assessment of risk at the overall level of the Bank and the level of the activity and single transaction is based on several structured methodologies, some based on expert assessments in area of activity, and some, on the basis of historical data and statistical models of various types. The changes in the risk environment in Israel and around the world, as well as the changes in the perception of risk, require the Bank to revise its assessments and the methodologies it employs, while constantly being challenged by the interested parties.

Risk environment and its impact on the Bank

In 2013, the risk environment moderated compared to 2012, against a background of an improvement in the United States economy and stabilization in Europe, led to a reduction in the prospects of the realization of a global stress scenario. However, looking forward, the recovery in Europe is not yet complete. The exit process of the United States central bank from a policy of purchasing the assets is the result of the improvement in the economy, but it has entered a new dimension of uncertainty in markets, with an emphasis on an increase interest risk and asset prices.

Business factors and the Risk Management Division are monitoring these developments and are taking decisive steps specifically to minimize the risks.

The main risk areas which are expected to impact the Bank's activities in the coming year are as follows:

1. **Slow recovery in the world economy, slowdown in the local economy and markets**

   Global economic slowdown in recent years, with an emphasis on the economy of Europe, leads to a slowdown in the growth of the local economy. From the aspect of credit, the local slowdown, combined with the continuing trend of appreciation in the exchange rate, affects customers of the Bank who are companies from various segments, in particular, exporters. The slowdown leads to a fall in demand for credit for financing business activity. On the other hand, the low level of interest eases the financing requirements of the customers. However, a scenario of rapidly increasing interest rates is liable to hamper them in this context. From the aspect of exposure to market risks, the global economic environment is likely to continue to be reflected in volatility on financial markets and throughout the coming year and affect the Bank's investments in securities in the nostro portfolio.

2. **Compliance risk**

   The risk of non-compliance with the provisions of the law in the widest sense as outlined above (hereinafter, "compliance risk") increased and it is expected to continue to be a central risk in the field of banking in Israel and around the world. In recent years, banks in the United States and in Europe have absorbed substantial penalties in respect of compliance risk in activity with customers, activity in the capital market and interest rates and in respect of activity in the area of private banking. In addition, the frequent changes in regulations require constant pro-active monitoring and assessments within a short time-framework, which require the allocation of several resources.

3. **Tighter regulatory requirements**

   Since the financial crisis in 2008, the requirements on banks, in Israel and around the world, have become stricter, against a backdrop of the lessons absorbed and still being learnt from the crisis. The main changes, as reflected in the Basel III directives dealt mainly with the strengthening of capital and liquidity of the banks in Israel and around the world. The impact of these regulatory requirements on the banking system in the world, and in Israel, as well, is considerable. At the same time, there has been an increase in additional initiatives for reforms in the banking system, which are likely to affect the Bank's activity and its profits.

4. **Domestic real estate market**

   The local real estate market, with an emphasis on housing, has been characterized by significant price increases in recent years. The main concern in this area is that the low interest environment supports high price levels and when interest rates begin to rise, real estate prices will fall considerably, causing a stress scenario of a crisis in the sector that will spread throughout the economy. This fear is also reflected in the annual report of the International Monetary Fund, published in February 2014.

   Leumi reduces its exposure to risk of credit because of a fall in real estate prices by the implementation of structure underwriting policy and other routine monitoring of the development of the risk in the sector. In 2013, there was fall in concentration of real estate credit in the Leumi portfolio.

5. **Risk of cyber attacks**

During the past year, a number of cyber events materialized in Israel and around the world. The realization of this risk compels banks to invest a great deal of resources in defending against data protection risks including cyber risks, both in specialist personnel, and in intelligence and infrastructures, in order to reduce exposure to this risk. Adverse changes in the geopolitical environment also act to increase the risk from cyber attacks, as the virtual arena has become one of the leading war zones for organizations and states.

Definition of severity of the risk factors

The methodology for classifying the degree of severity of exposures to the various risks, as outlined in the table of severity of risk factors, is based on estimating exposure to the various risks and the quantification of the impact of the scenarios materializing on the Group's capital, i.e., its stability. The degrees of severity defined below are based on potential stress scenarios and present the level of exposure divided into three levels: low, medium and high. This is as a function of the extent of the impairment, in relation to the Group's capital in the event of the risk materializing. Impairment of up to 1% in Tier 1 capital adequacy is defined as low risk; "medium" risk is defined as risk the realization of which is liable to lead to a fall in capital adequacy at a rate of more than 1%, but without reducing the capital adequacy ratio to below 6.5% and impairment that will lead to a fall in the capital adequacy ratio below 6.5% is defined as high risk.

It is important to note that the said methodology for assessing the severity of the risk factors is one of many employed by the Bank. The Bank regularly checks the effect of various events that may occur not only on capital adequacy and stability, but also on the current profit, on goodwill, etc. These assessments are discussed in a forum of members of management and in the Board of Directors.

The table of severity of risk factors presented below presents an assessment of the severity for each of the various risks derived from evaluating the effect of the realization of stress scenarios determined on the Bank’s capital adequacy. It should be noted that none of the exposures to the risk factors is defined as high or critical, and the breakdown of the risks obtained corresponds to the Group's risk appetite and goals.

With regard to the financial statements for 2012, no change took place in risk classification according to risk level, as the increase in the risk environment described above, in the section on Risk Environment and its Impact on the Bank, did not result in any significant change in the assessment of the effect of each risk factor on the Bank’s capital and its stability.

Some of the information included in this chapter is "forward-looking information". For an explanation of this term, see "Description of the Banking Corporation's Business and Forward-Looking Information" above.

Table of severity of risk factors

	Risk	Definition	Degree of severity *
1	Overall credit risk	Risk of a loss as a result of the possibility that a counterparty does not comply with its obligations. The reference is to credit to the public, derivatives, deposits in banks, investments in debentures and capital holdings.	Medium
1.1	Quality of borrower and securities risk	Amount of risk described by the likelihood of failure of borrowers, the loss given a failure, which is also affected by the collateral, and the exposure at a time of failure of individual borrowers.	Medium
1.2	Large borrower and group of borrowers concentration risk	Credit risk arising from the relative size of borrowers in the credit portfolio of the Bank.	Low
1.3	Industry and sector concentration risk	Credit risk arising from concentration of credit to borrowers in certain sectors and segments of the economy.	Medium
2	Overall market risk	Risk of exposure of the Group's assets to changes in exchange rates, interest, inflation and asset prices, the correlation between them and their volatility levels.	Medium
2.1	Base risk	Risk due to fluctuations of the exchange rate, including inflation (trading portfolio and banking portfolio).	Low
2.2	Interest risk	Risk due to fluctuation in interest rates (trading and banking portfolio)	Low
2.3	Margin and share prices risk	Risk as a result of fluctuations in share and bond prices in the commercial portfolio and in the banking portfolio for assets remeasured at market price.	Low
2.4	Liquidity risk	The risk of inability to withstand the uncertainty in relation to the possibility of raising funds and/or realizing assets, in an unexpected manner and within a short time-frame, without incurring a material loss.	Low
3	Operating risk	Risk of loss that can arise from weaknesses or failures in processes, large projects, people or systems, or external events. This risk includes legal risk, but does not include strategic risk or reputational risk.	Low
3.1	Legal risk	The risk arising from activity which does not correspond with legislation (civil), legal errors and class actions conducted against the Bank.	Low
3.2	Compliance risk	The risk that can arise from non-compliance with requirements of the authorities, which will be expressed in penalties on the Bank or on employees.	Low
4	Reputational risk	The risk that a negative publication would cause a fall in the customer base, a fall in revenues, liquidity or high legal costs.	Low
5	Holistic systemic risks	Risks caused as a result of external events that could lead to the materialization of a number of risks simultaneously.	Medium

* In relation to potential impairment in capital adequacy.

Definitions of risks in the above table:

1. Credit risk

The risk of loss resulting from the possibility of a borrower not meeting its obligations. This refers to credit to the public, derivatives, bank deposits, investments in debentures, and holdings in equity. The severity of overall credit risk is medium. (For further details on risk management, see below in this chapter.) Details of sub-risks included in the definition of credit risk according to the Group mapping are as follows:

1.1 **Risk in respect of a single borrower and collateral**: The risk of the entry of a counterparty into default, leading to failure to meet contractual monetary obligations. The risk includes:

- Entry into default of counterparty in derivatives.
- Residual risk in respect of inability to realize collateral.
- Country risk deriving from the exposure of borrowers operating in foreign countries.
- Credit risk in shares deriving from the exposure to default in respect of a holding of shares for investment purposes.

The level of severity is defined as medium.

1.2 **Concentration risk:** Credit risk in a significant exposure to borrowers with similar economic characteristics or who are engaged in similar activities or under the control and/or management of a certain factor, which may lead, in a situation of change in the economic situation, to a similar effect on the ability to meet debt repayments of those borrowers. Below are details of sub-risks included in the definition according to the Group mapping:

1.2.1 Significant exposure to a large borrower or group of borrowers. The severity of the risk level is defined as low;

1.2.2 Sectoral and segmental exposure. The severity of the risk is defined as medium;

The severity of the overall risk and sub-risks was examined in the framework of stress scenarios which reviewed what damage there was in respect of concentrations of credit in the portfolio as a result of a serious crisis occurring. The severity of overall concentration risk is assessed as medium.

2. Market risk

Market risk is defined as a risk of exposure of Group assets because of uncertainty of changes in exchange rates, interest, inflation and shares, the correlation between them and their level of volatility. The severity of overall market risk is medium. For further details on risk management, see below in this chapter.

2.1 Basis risk. The severity of the risk is defined as low;

2.2 Interest risk. The severity of the risk is defined as low;

2.3 Bond margin and share prices. The severity of the risk is defined as low.

The severity of the general risk and sub-risks was evaluated in accordance with the most severe stress scenario in the set of scenarios for these risks. The severity of overall market risk is defined as medium.

2.4 **Liquidity risk**: Uncertainty with regard to the possibility of raising funds and/or realizing assets, unexpectedly within a short timeframe, without causing material loss. This risk has been determined as low, since the Bank complies with the liquidity ratios that it sets for itself, including probability indices, and the subsidiaries also comply with the indices that they have set for themselves. Monetary damage in a very severe liquidity scenario is also low.

3. Operational risk

Operational risk is the risk of a loss resulting from inadequate or failed internal processes, people or systems, or external events. This risk includes legal risk, but excludes strategic and reputational risks. The evaluation of the level of severity relates to damages at a high level of severity and a review of historical events. The level of severity of the risk is defined as low. For more information on management of the risk, see below in this chapter.

3.1 Legal risk:

The risk of loss resulting from the inability to legally enforce the performance of an agreement or contingent liability. The definition includes risks deriving from legislation, regulations, case law and regulatory directives, risks deriving from operations not backed by adequate agreements or without legal counseling or according to deficient legal counseling. A plan for managing legal risks is implemented in the Group whose objective is to identify, prevent, manage and minimize legal risks. In view of the results of an analysis of the legal consulting division for a potential stress scenario, the Group's legal risk is categorized as low. For more information on management of the risk, see below in this chapter.

3.2 Compliance risk:

The risk that may derive from non-compliance with regulatory requirements and laws of the various authorities in Israel and abroad. The level of severity for compliance risk within the Group is defined as low.

4. Reputational risk

The risk that the publication or public disclosure of a transaction, a party to a transaction or customer-related business practice, as well as business results and events pertaining to the Group, may have an adverse impact on the public's confidence in the Group. The Group’s reputational risk is managed by maintaining high levels of compliance with the various regulatory provisions, maintaining high levels of control, and orderly work procedures by the management and the Board of Directors and their ability to monitor the current operations. Leumi has a code of ethics governing conduct *vis-à-vis* employees, suppliers and the environment. Leumi Group ensures that the products and services it supplies are of the highest quality. The treatment of employees and customers is reflected in the minimal number of complaints. In addition, there are detailed contingency plans for dealing with reputational events. The level of severity of reputational risk is defined as low.

5. Holistic systemic risks

Risks deriving from economic, political, and geopolitical events in Israel or abroad that may endanger the stability of the Group, such as a war or a global economic crisis. The assessment of the risk is based on the total loss in a very severe stress scenario in the Group's set of scenarios including the occurrence of a number of risks together. The degree of severity of risk in Leumi is defined as medium.

Basel Directives and Assessments in Leumi

The data in Leumi's financial statements, the calculation of the risk assets and the capital adequacy ratio as at 31 December 2013 are calculated and presented in accordance with the principles of the standardized approach in Basel II. The capital adequacy ratio of 14.82% presented by Leumi at 31 December 2013 according to assessments of the Group covers the required capital in respect of the First Pillar and the Second Pillar, including the stress scenarios used by the Group in its internal assessments.

In this report, certain data required by Pillar 3 have been expanded and/or added in accordance with the instructions of the Banking Supervision Department, as detailed below:

Subject	Table	Directors' Report	Financial Statements
General	1	Page 12	-
Capital Structure (Qualitative and Quantitative)	2	Page 22	Note 13
Capital Adequacy (Qualitative and Quantitative)	3	Page 24	-
Risk Exposures and Assessment – General Qualitative Disclosure		Pages 165-169	
Credit Risk Qualitative Disclosure	4(a)	Pages 176-177	-
Credit Risk Exposures by Principal Types of Credit	4(b)	Page 179	
Exposures by Geographic Area to Foreign Countries	4(c)	Page 199	Exhibit F
Credit Risk Exposures by Third Party and Principal Types of Credit	4(d)	Page 180	
Credit Exposures by Repayment Period	4(e)	Page 181	
Problematic Credit Risk Exposures and Provision for Doubtful Debts by Economic Sector	4(f)	-	Exhibit E
Total Impaired Loans and Provisions by Geographic Area	4(g)	-	Exhibit F
Movement in Balances of Allowance for Credit Losses	4(h)	-	Note 4A.1
Credit Exposures by Risk Weighting	5	Pages 182-185	
Mitigation of Credit Risk (Qualitative and Quantitative)	7	Pages 186-188	-
Credit Exposures in Derivatives by Counter Party (Qualitative and Quantitative)	8	Pages 189-192	-
Securitization (Qualitative and Quantitative)	9(f), 9(g)	Pages 90-91	Note 3
Market Risk (Qualitative and Quantitative)	10	Pages 202-210	-
Operational Risk - Qualitative Disclosure	12	Pages 213-216	-
Investment in Shares (Qualitative and Quantitative)	13(b)	Pages 93-94	-
Investment in Shares of Companies Included on Equity Basis	13(b)	Pages 139	-
Interest Risk	14	Pages 207-208	Exhibit D

ICAAP (Internal Capital Adequacy Assessment Process)

The process of assessing capital adequacy serves to examine the capital required for supporting the various risks to which the Group is exposed, in order to ensure that the Group's capital actually exceeds the said capital requirements at any time. As part of the process, the risk appetite and the risk-bearing capacity were defined, a comprehensive process of mapping and assessment of risks to which the Group is exposed is carried out, a comprehensive framework for analyzing stress scenarios in the context of the management of the Group as a going concern was developed, and processes of managing the risks and the risk management structure in the Group were examined.

The results of the process were formally collated in the ICAAP document which was submitted to the Supervisor of Banks in April 2013. This process was examined by the Supervisor of Banks as part of the Supervisory Review Process (SREP). The updated ICAAP document for this year is currently being updated and will be submitted in April 2014.

Basel III

In June 2011, the Basel III directives "Increasing the Resilience of the Banking System" (published in December 2010) were updated by the Bank for International Settlements (BIS). These directives rely on the Basel II directives and update several aspects learned from the lessons of the recent financial crisis. Final directives for the implementation of Basel III were also published in the European Union and in the United States. In the European Union, the directives came into force at the beginning of 2014, and in the United States, they will be applied at the beginning of 2015 for most banks, and partly in 2014, with regard to the major banks.

The purpose of the directives published by the BIS is to reinforce the standing of the banking system at a time of crisis, in view of the lessons learned from the crisis of 2008-2009, introducing improvements in the area of risk management and with an emphasis on:

- Improving the quality of capital and an increase therein.
- Improving the liquidity ratios and determining consistent standards for measuring liquidity.
- Reducing the pro-cyclical influence of the economic situation on the capital requirements.
- Increasing transparency of the risk management methods.

From the aspect of capital, the directives focus on a renewed definition for the components of capital and the determination of higher minimum capital adequacy ratios.

Implementation of Basel III in Israel

On 30 May 2013, the Supervisor of Banks issued final directives for the adoption of Basel III recommendations in Israel, through an amendment of Proper Conduct of Banking Business Regulations 201-211. The directives came into force on 1 January 2014.

Regarding Proper Conduct of Banking Business Regulations 201, "Measurement and Capital Adequacy, Introduction, Scope of Application and Calculation of Requirements", all banking corporations are required to comply with a minimum Tier 1 shareholders' equity ratio of 9%, by 1 January 2015. In addition, a large banking corporation, with total balance sheet assets on a consolidated basis representing at least 20% of the total balance sheet assets of the Israeli banking system, will be required to comply with minimum Tier 1 shareholders' equity ratio of 10%, by 1 January 2017. This additional regulation applies to Leumi.

In addition, all banking corporations in Israel will be required to comply with an overall capital ratio of 12.5%, with effect from 1 January 2015. A large banking corporation will be required to comply with an overall capital ratio of 13.5%, with effect from 1 January 2017. This additional regulation applies to Leumi.

The following is a number of additional points of emphasis from the Bank of Israel directives for the adoption of Basel III directives:

1. Tier 1 shareholders' equity was redefined and a number of changes made in its components, including:

   A capital reserve in respect of available-for-sale securities (after tax) will constitute a part of Tier 1 shareholders' equity, whether it is positive or negative;

   For recognition of minority interest, a restriction has been added, which is dependent on capital surpluses in the investee company;

   A dividend which is declared after the balance sheet date will not be deducted from Tier 1 shareholders' equity, in contrast to the Basel II directives.

   A different structure of deductions from capital, and a number of new deductions have been established, as set forth in Proper Conduct of Banking Business Regulations 202 "Measurement and Capital Adequacy – Regulatory Capital".

2. The distinction between Upper Tier 2 capital and Lower Tier 2 was canceled, as was Tier 3. However, the restriction whereby Tier 2 capital must not exceed 100% of the Tier 1 shareholders' equity was retained, and the qualifying capital instruments to be included in Tier 2 capital must not exceed 50% of the Tier 1 shareholders' equity (after the required deductions from this capital). This restriction does not include the capital instruments that were included prior to the effective date of this regulation in Upper Tier 2 capital, subject to transitional provisions.

3. Eligibility criteria are provided for Tier 1 capital and Tier 2 capital, including the requirement that the instruments have a mechanism for absorbing losses when there is a fall in certain Tier 1 shareholders' equity adequacy requirements. The inventory of the existing capital instruments when the Basel III requirements become effective will gradually be deducted from the capital base.

   A description of the main characteristics of regulatory capital instruments that have been issued is presented on the Bank's website /hhtp://leumi.co.il/home01/32587

4. A collective allowance for credit losses, before the effects of tax, will be recognized as part of Tier 2 capital, up to 1.25% of weighted risk assets in respect of credit risk according to the standardized approach.

5. A surplus investment in a single non-bank corporation of more than 5% of Tier 1 shareholders' equity will receive the proportion of risk of 1250%.

6. The capital requirement has been provided in respect of CVA (credit valuation adjustment) losses that may be incurred as a result of a deterioration in the quality of the credit of a counterparty in an OTC derivative transaction.

7. A transitional period of four years has been provided for the full implementation of the Basel III requirements.

8. Assuming the full and immediate implementation of the Bank of Israel directives, relating to the adoption of the Basel III directives (without taking into account the transitional provisions), the Tier 1 shareholders' equity ratio of Leumi Group as of 31 December 2013 was 9.05%, compared with 9.43%, according to the Basel II directives. This result is based, *inter alia*, on the Bank's interpretations of the directives.

9. Assuming gradual implementation, according to the transitional provisions, of the Bank of Israel directives, relating to the adoption of the Basel III directives, the Tier 1 shareholders' equity ratio of Leumi Group as of 31 December 2013 was 9.20%, compared with 9.43%, according to the Basel II directives. This result is based, *inter alia*, on the Bank's interpretations of the directives.

The table below set forth the principal factors and the expected changes therein in capital adequacy of Leumi Group as of 1 January 2014 due to the implementation of the Basel III directives, in accordance with the transitional provisions.

a. Capital components

	Change in Tier 1 shareholders' equity	Change in overall capital	Effect on Tier 1 shareholders' equity adequacy ratio	Effect on overall capital adequacy ratio
	NIS millions		Percentages	
Inclusion of the capital reserve in respect of available-for-sale securities in Tier 1 shareholders' equity	**181**	**81**	**0.06**	**0.03**
Non-recognition of minority interests in surplus capital of subsidiaries consolidated	**(40)**	**(37)**	**(0.01)**	**(0.01)**
Cancelation of the de from capital of investments in banking and financial subsidiaries not consolidated and cancelation of deductions related to securitization exposure	**65**	**129**	**0.02**	**0.04**
Inclusion of the collective allowance for credit losses in Tier 2 capital	**-**	**2,272**	**-**	**0.82**
Reduction from Tier 2 capital of liability notes which are not eligible as regulatory capital, pursuant to the transitional provisions	**-**	**(2,909)**	**-**	**(1.04)**
Other effects	**(49)**	**(49)**	**(0.01)**	**(0.02)**
Total	**157**	**(513)**	**0.06**	**(0.18)**

b. Risk assets

	Risk assets	Effect on Tier 1 shareholders' equity adequacy ratio	Effect on overall capital adequacy ratio
	NIS billions	Percentages	
Deferred taxation in respect of timing differences	**3.93**	**(0.13)**	**(0.20)**
Counterparty risk in derivatives (CVA)	**2.35**	**(0.08)**	**(0.12)**
Collective allowance added to Tier 2 capital	**1.84**	**(0.06)**	**(0.10)**
Other effects	**0.44**	**(0.02)**	**(0.02)**
Total	**8.56**	**(0.29)**	**(0.44)**

On 13 January 2013, the Bank of Israel published an amendment to Proper Conduct of Banking Business Regulation no. 342 regarding the management of liquidity risk. The directive represents a milestone in the adoption of the international regulatory directives regarding liquidity. The purpose of the revised regulation is to begin gradually to adopt the Basel III directives for managing liquidity risks, and at its center, is the definition of minimum ratios between liquid assets and liabilities which, it is estimated, will materialize within a specified time period. In particular, it involves the definition of minimum ratios between liquid assets and liabilities which, it is estimated, will materialize within a specified time interval. In particular, this involves the definition of a minimum liquidity ratio for a period of a month (a liquidity coverage ratio - LCR) and the definition of stable funding ratio for a period of a year (a net stable funding ratio - NSFR). The Bank calculates the liquidity ratios in accordance with the Bank of Israel directives. In February 2014, the Bank of Israel requested the implementation of a quantitative impact survey (QIS) to assess the effect of adopting the Basel III directives on the banks' liquidity ratios.

On 30 May 2013, the Bank of Israel published the provisions of Proper Conduct of Banking Business Regulation No. 333 for Interest Risk Management, which is based mainly on the principles of Basel for the management of interest with the required adjustments. At the center is a directive requiring qualitative controls, the segregation of duties and the use of stress scenarios and advanced models for interest risk management. The directive will come into force on 1 July 2014. The Bank is prepared for the timely implementation of the directive.

Credit risks

Credit risk is the risk of the Bank incurring a loss as a result of the possibility that a borrower or counterparty of the banking corporation does not meet its liabilities *vis-à-vis* the banking corporation, as agreed.

The Bank's credit and credit risk policy document gives major expression to the Bank's credit risk strategy. This is together with the existing procedures for identifying, measuring, monitoring supervising and controlling the credit risk. The credit policies and procedures currently in force relate to the credit risks in all of the Bank's activities, and apply both to the single credit and to the entire credit portfolio.

In addition to the Bank's credit policy document, there is a credit and credit risk policy document at the Group level which outlines the framework and supra-principles for the policy documents of each of the Group companies in Israel and abroad (the United States, the United Kingdom and Romania). The Bank's credit policy, representing a recommendation and guideline for crystallizing the Bank's credit policy in each of the subsidiaries in Israel, is also presented for the subsidiaries in Israel.

The supplement to of all the above is a document relating to business goals, as determined by management, forming a basis for the Bank's work program.

The Bank's credit and credit risk policy document in Israel is updated each year, discussed by the Bank management and approved by the Board of Directors of the Bank. The document outlines policy for the Bank's activity in Israel and gives expression to the state of the economy in the world and in Israel and to the risk environment evaluated for the coming year. The guiding principles in the Bank's credit policy are based on the dispersal of risks and their controlled management. This is reflected in the diversification of the credit portfolio among the various sectors of the economy and over a large number of borrowers.

The principles guiding the Bank include:

- Focusing on exposures in activities where the Bank has the expertise required to assess and manage the inherent risks.
- Involvement with varying types of credit with the aim of achieving risk dispersal.
- For each credit risk, there should be segregation between the unit dealing with the credit risk and an independent unit exercising control over the credit risk and over the management of the credit risk.
- Preparing a risk analysis before starting new lines of business or launching new products.
- The segmentation principle: allocating the handling of customers along business lines is carried out according to the operating turnover of the customer and the size of the obligo facility available to him, and according to the complexity/specialization of the type of transaction.
- Every unit in the Bank that creates exposure to credit risk and manages it must be aware of the risks in the area of its operations and responsible for its routine management. This includes awareness and risk management in the area of compliance likely to accompany transactions (credit, liabilities to customers and routine activity).
- Carrying out routine and periodic control of credit exposures, with the aim of identifying weaknesses as early as possible and taking the appropriate steps.
- Evaluating credit risk in a quantitative manner, and deciding on a risk rating for every customer. To achieve this aim, the Bank has models and automated systems for supporting the process of reviewing the risk level of the borrower, and evaluating the expected loss.
- Determining an outline operating plan that creates differentiation between three types of activities:
    - Activities/segments with a low level of risk which the Bank is interested in financing and would like to expand;
    - Activities/segments with a medium level of risk, in which the financing is selective.

- Activities/segments with a high level of risk which the Bank tends to avoid because of the increase of exposure.

  Details of the outline operating plan are presented in the Credit Policy Document of the Bank and are updated once a quarter as necessary.

- Determining, managing and monitoring internal quantitative limits. In addition, the distribution of risk ratings of borrowers in the Bank is monitored by various cross-sections.
- The Bank has been working for a number of years to increase vigilance and general awareness among customer managers and the potential negative implications of the environmental aspects on projects it finances. The Bank takes steps to identify the sensitive industries and to integrate a component of this exposure when making credit decisions.

Control and management procedures

In the area of credit management, the procedures for the control and supervision of risks have improved, *inter alia*, by the establishment of centers of expertise for the area of credit in the Retail Division, the merger of mortgage activity in the Banking Division and the intensification of the "segmentation" of corporate customers in the appropriate lines of business and in the framework of specialist branches.

The examination of the credit frameworks of the Bank's large borrowers and the approval of the transactions or their transfer for discussion within the appropriate credit committee have been carried out for a number of years, with the involvement of Credit Risk Management (CRM) units, which were, as aforesaid, transferred at the beginning of 2014 to the aegis of the Risk Management Division. This transition, which was in compliance with the requirements Banking Supervision Department, will strengthen the independence and autonomy of the CRM units, and will support better synergy between the individual consideration and the management at the total Leumi portfolio level, while streamlining the credit processes.

For further details, see paragraph "Organizational structure and management responsibility for credit risks".

As part of the control and supervision over credit, there are directives and regulations relating to the type of credit, terms of financing, method of reliance on the various collaterals, type of transaction and periods of credit, in the context of which the control and supervision over executing policy were tightened. On the individual level, special emphasis has been placed on the examination of the business condition among customers whose risk level has increased. Control is exercised by the use of control tools and improvement in the efficiency of working procedures. The Bank maintains a constant review of the effect of erosion and exposures created among the relevant borrowers, including intense discussion regarding customers defined as sensitive.

Managing the loan portfolio in the Bank requires, *inter alia*, having a quantitative assessment of the risk level of the borrowers. To achieve this aim, models and automatic systems have been implemented in the Bank to support the process of examining the risk level of the borrower, the expectancy of loss, and the return required for these risks.

The Bank employs an advance system for managing the loan portfolio, with the aim of upgrading its capability to control the various risks, and particularly credit concentrations, maintaining the limits on risk factors in the area of credit, directing activities with the objective of improving the ratio of return on risk, and facilitating a more accurate pricing system of credit risks.

As stated, the Board of Directors of the Bank approves the Bank's credit policy (including the policy with regard to collateral) and internal limits - sectoral and other.

Outline according to economic sector

As part of policy, three categories of economic sectors are specified according to the risk rating of each sector – the sectors at a low, medium and high level of risk. This outline plan is routinely updated in accordance with periodic analyses of the various sectors and segments of the economy according to the risks and prospects inherent in each sector. The sector outline plan represents a further consideration in specific decisions regarding the grant of credit, together with an individual examination of risk features of the borrower/transaction and its risk rating.

For further details on this subject, see the paragraph on "Credit concentration".

Credit policy in overseas subsidiaries

In each of the Bank's overseas units, the subsidiary's credit policy is approved by the local board of directors. A summary description of credit and the main characteristics of the credit portfolio in the overseas units are presented once every period to the Board of Directors of the Bank in Israel.

As in Israel, the credit policy of overseas subsidiaries is based on spreading risks, while setting limits for exposure in the various sectors of the economy and operating segments. However, the level of sectoral concentration in the subsidiaries is higher, compared with the Bank in Israel, due to their relative small size and the need to focus on specific niches. In addition, collateral policy is prescribed within the scope of the credit policy, including principles and rules regarding the various types of collateral, the extent of reliance thereon, etc. This is done in accordance with and subject to all the banking regulations and directives of each country. Various levels of credit-granting authorities are set for each subsidiary. In addition, in those subsidiaries providing commercial credit, there is a process for rating borrowers according to levels of risk and in subsidiaries with a substantial credit volume, there is a loan review unit which performs routine examinations of the risk level of the Bank's customers.

Reporting on credit risk

The Bank is meticulous in maintaining routine and up-to-date reporting to members of the Bank Management, the Board of Directors and the Banking Supervision Department. Reporting to the Banking Supervision Department includes reports on various credit matters, including credit risk by sectors of the economy, financial instruments, the structure of shareholders' equity and the minimum capital ratio, large individual borrowers and groups of borrowers, credit for financing the acquisition of means of control, problem loans, and supplementary provision, credit exposures of subsidiaries abroad, related persons, etc.

Reports to Bank Management and to the Board of Directors relate to the development of credit for exceptional or major transactions, the results of quarterly reviews of the breakdown of the credit rating of borrowers, in particular, and of the overall credit portfolio in general, quarterly reports on concentrations of credit by sector of the economy, individual borrowers and groups of borrowers, loans for financing the acquisition of means of control, countries, Israeli and foreign banks in relation to the limits set by the Banking Supervision Department and internal limits, the distribution of problem credit among the various units of the Bank, and information on particularly sensitive customers, etc.

Organizational structure and management responsibility of credit risk

Risk management functions

There is a dedicated risk management culture in the Leumi Group which is the key to effective risk management. The Board of Directors prescribes the risk management processes and risk appetite of the Group on the basis of suggestions brought by the management.

Risk management in the Bank is based on three lines of defense, i.e., risk management is effected at the different levels of authority and responsibility in the three lines of defense.

First line – Business lines

The business units (first line of defense), whose activity is involved in credit risk taking, in an appropriate risk environment, in the framework of which credit management and operation processes were defined. Control activity is an integral part of the risk management process. The process of credit approval is carried out in accordance with the Bank's credit policy and in accordance with the scale of authorities that has been established.

Credit and risk management centers – in the Banking Division

In 2012, an organizational change was made in the Banking Division, the assimilation of which was intensified and completed in 2013, such that the professional functions related to credit risk were removed from the responsibility of the regional managements, and are now managed in "credit centers". These are independent units, reporting directly to the divisional risk manager and manned by professional and experienced credit officers. Each credit center operates with the branches in the regions defined within its area of responsibility, and deals with each credit approval beyond the authority of the branches (some under the authority of the center itself, and some, transferred to be dealt with by the division management).

Furthermore, the center is engaged in aspects of monitoring and credit control, regulating and supervising the branches' activity in this area, aspects which have been expanded and established during the past year.

Special Credit Department

The Special Credit Department operates under the responsibility of the Head of the Credit and Real Estate Division. The department specializes in dealing with customers in difficulty from the commercial banking and corporate banking segments, and consists of the following two sectors:

1. **ITSC (Intensive Treatment of Sensitive Customers) Sector** – a professional unit dealing with active customers presently in difficulty, under the assumption that the company can be brought back to normative operations if it is correctly managed and financed.
2. **Collections Sector** – deals with inactive customers or those whose operations are about to be shut down. The two sectors above are often aided by relevant external parties such as external lenders, accountants, architects/engineers, lawyers, etc.

Second line – Risk Management Division

As a rule, the responsibility of the Risk Management Division is to formulate risk policy and limits for the approval of the Board of Directors, to develop and challenge the assessment or risk in material transactions and new activity and analyze all of the risks in the credit portfolio with a collective vision. This was in order to assist the management to advance an integrated corporation-wide perspective of risks. As aforesaid, at the beginning of the chapter, with effect from 2014, the responsibility for analyzing risks in specific loans whose amount exceeds NIS 25 million, and the overall responsibility of the appropriateness of the classifications and allowances has been transferred to the Risk Management Division.

Credit Risk Management (CRM) Department in the Risk Management Division

The activity and designation of the CRM units are to take steps for the optimization of decision-making in credit portfolios. CRM units are responsible for the in-depth analysis of credit applications from business units, validating borrowers' risk ratings (assessment of the internal risk), carrying out a periodic review in conjunction with the business units with regard to particularly sensitive borrowers, making recommendations on classifications and provisions. Alongside this, the CRM units, in conjunction with the credit risk section and managements of the corporate divisions, are working to develop methodologies and financing "formats", develop control processes and assimilate working procedures and rules for granting credit at Bank level. The main work of the units focuses on making an independent examination of customer relations managers' recommendations for determining or for extending credit facilities for financing customers under their care, and identifying customers whose situation has deteriorated, while indicating the main risks characterizing the credit portfolio and making recommendations for the continued customer service. As part of the rationale behind the establishment of the Credit Risk Management units, and with the aim of improving and simplifying the decision-making process and shortening timeframes for providing credit, a change was made in the hierarchy of credit authorities at the various levels so that some credit applications are approved by the business factors, subject to conditions stipulated by Credit Risk Management units. This allows the credit committees to devote more time to discussing borrowers characterized by a high level of exposure, and to complex transactions.

The CRM units provide a solution for transactions of over NIS 25 million of the Commercial, Corporate and Real Estate Department. Reporting to the Real Estate Credit Risk Management unit is an "Appraisals Department", whose duties, *inter alia*, are to examine and validate appraisals of real estate assets pledged to the Bank (in excess of the specified threshold amount), carried out by certified appraisers, and to determine the maximum collateral value of the properties.

Credit risk management section in the Risk Management Division

The Credit Risk Department operates in the Risk Management Division, which reports to the Chief Risk Officer of the Group (CRO). The department is responsible for credit risk management at the total credit portfolio level, including the formulation of the credit and credit risks policy document for approval by management and the Board of Directors, monitoring and analyzing risks in the entire credit portfolio, independently examining and controlling specific credit portfolios and developing quantitative models and tools for measuring and controlling credit risks.

Third line – Internal Audit

Its function is to examine (usually post facto) the correctness and effectiveness of the risk management process in accordance with the Bank's targets and to expose weaknesses in internal controls.

Tools for credit risk management

In managing credit risk, use is made of quantitative models for rating the risk of borrowers and for evaluating and monitoring the risk at portfolio level.

The grant or renewal of retail credit (private and small business customers) up to a defined maximum sum is examined under a credit-scoring system, according to which the level of risk of exposure to the customer's activity is estimated over time in the account. Corporate and commercial credit (transactions above the abovementioned ceiling) and major private customers are rated under the credit rating system which operates at the Bank. This credit rating assists management in the decision-making process, in pricing the credit, and in monitoring its quality over time. Credit risk is dependent on the probability of default by the borrower within one year of the rating in a given period, or PD (probability of default), the extent of the exposure in respect of the borrower at the time of default, EAD (exposure at default), and the loss from the borrower in a given default, or LGD (loss given default). The borrower evaluation system, coupled with the system for measuring profitability from the customer, provides a basis for connecting the level of risk and the pricing for the customer and improving various routine management aspects.

At the portfolio level, the Bank is assisted by an economic capital model, which is based on the rating of the borrowers, in order to assess the credit risk at the level of the total credit portfolio and at its different cutoffs.

Conclusion-drawing process

The Bank has a process for drawing conclusions on credit matters, with the participation of the managers of the various units of the Bank. Committees for drawing conclusions have been established in the various divisions for this purpose. These committees convene periodically in order to discuss incidents of default, analyze the implications and significance of the findings of the incident, and formulate recommendations for improving work processes and enhancing business efficiency. The recommendations accepted by the committees are, where necessary, implemented in revisions to credit and collateral policy, in amendments to working procedures at the Bank, and in updates of training programs.

Capital requirements in respect of credit risk

For information regarding the capital requirements in respect of credit risk pursuant the Basel II directives, the standardized approach, see the chapter, "Capital Resources and Capital Adequacy".

Risk exposures according to main type of credit exposure (Table 4(b) - Basel II):

	31 December 2013	31 December 2012	**31 December 2013**	31 December 2012
Type of credit exposure	Gross credit risk exposures		Average gross credit risk exposures	
	NIS millions			
Credit	**287,212**	297,282	**288,773**	291,169
Debentures	**50,539**	43,043	**45,309**	42,445
Others	**15,724**	15,530	**15,904**	14,531
Guarantees and liabilities on account of customers	**120,159**	117,189	**118,620**	117,487
Transactions in derivative financial instruments	**8,116**	6,396	**7,139**	7,072
Total	**481,750**	479,440	**475,745**	472,704

Credit risk exposure by counterparty and by main type of credit exposure (Table 4(d) - Basel II):

	31 December 2013					
	Credit	Bonds	Others	Guarantees and other obligations	Transactions in financial derivatives	Total
	NIS millions					
Sovereign debts	**33,607**	**35,932**	**-**	**179**	**194**	**69,912**
Debts of public-sector entities	**5,317**	**5,680**	**-**	**92**	**31**	**11,120**
Debts of banking corporations	**9,463**	**3,508**	**-**	**2,064**	**2,995**	**18,030**
Debts of securities company	**-**	**176**	**-**	**-**	**-**	**176**
Debts of corporations	**99,714**	**3,072**	**-**	**75,310**	**4,795**	**182,891**
Debts collateralized by commercial real estate	**20,621**	**-**	**-**	**2,259**	**-**	**22,880**
Retail exposures to individuals	**33,724**	**-**	**-**	**29,627**	**95**	**63,446**
Loans to small businesses	**15,274**	**-**	**-**	**4,586**	**6**	**19,866**
Housing mortgages	**69,492**	**-**	**-**	**6,042**	**-**	**75,534**
Securitization	**-**	**2,171**	**-**	**-**	**-**	**2,171**
Other assets	**-**	**-**	**15,724**	**-**	**-**	**15,724**
Total credit risk	**287,212**	**50,539**	**15,724**	**120,159**	**8,116**	**481,750**

	31 December 2012					
	Credit	Bonds	Others	Guarantees and other obligations	Transactions in financial derivatives	Total
	NIS millions					
Sovereign debts	41,551	30,875	-	217	27	72,670
Debts of public-sector entities	4,339	4,057	-	114	19	8,529
Debts of banking corporations	11,193	2,947	-	2,100	2,170	18,410
Debts of corporations	110,427	3,443	-	74,779	4,093	192,742
Debts collateralized by commercial real estate	23,192	-	-	2,044	-	25,236
Retail exposures to individuals	29,941	-	-	27,998	84	58,023
Loans to small businesses	13,795	-	-	4,164	3	17,962
Housing mortgages	62,844	-	-	5,773	-	68,617
Securitization	-	1,721	-	-	-	1,721
Other assets	-	-	15,530	-	-	15,530
Total credit risk	297,282	43,043	15,530	117,189	6,396	479,440

Breakdown of portfolio by repayment period and by main type of credit exposure – (Table 4(e) – Basel II):

	31 December 2013					
	Credit	Bonds	Others	Guarantees and other obligations	Transactions in financial derivatives	Total
	NIS millions					
Up to one year	**139,737**	**28,742**	**3,486**	**75,294**	**4,811**	**252,070**
From one to five years	**69,172**	**9,692**	**951**	**27,521**	**5,558**	**112,894**
More than five years	**77,815**	**12,105**	**3,152**	**17,344**	**7,019**	**117,435**
Non-monetary items	**488**	**-**	**8,135**	**-**	**3,778**	**12,401**
Benefits to be offset	**-**	**-**	**-**	**-**	**(13,050)**	**(13,050)**
Total	**287,212**	**50,359**	**15,724**	**120,159**	**8,116**	**481,750**

	31 December 2012					
	Credit	Bonds	Others	Guarantees and other obligations	Transactions in financial derivatives	Total
	NIS millions					
Up to one year	156,095	20,874	2,796	75,118	4,364	259,247
From one to five years	68,517	13,879	1,427	26,576	4,794	115,193
More than five years	72,350	8,290	2,972	15,495	6,641	105,748
Non-monetary items	320	-	8,335	-	2,340	10,995
Benefits to be offset	-	-	-	-	(11,743)	(11,743)
Total	297,282	43,043	15,530	117,189	6,396	479,440

Credit risk in accordance with the standardized approach (Table 5 – Basel II)*:

The tables below give details of credit exposure according to risk weighting, allocating the exposure by counterparty, before and after mitigation of credit risk in respect of recognized collateral.

* See Tables 4(b) and 4(d) above for details.

Amount of exposure before expenses in respect of credit losses, and before mitigation of credit risk (2):

	31 December 2013											
	0%	20%	35%	40%	50%	75%	100%	150%	225%	650%	Deduction from equity	Gross credit exposure (1)
	NIS millions											
Sovereign debts	67,073	2,183	-	-	359	-	297	-	-	-	-	69,912
Debts of public-sector entities	-	5,214	-	-	5,905	-	-	1	-	-	-	11,120
Debts of banking corporations	715	13,210	-	-	3,137	-	968	-	-	-	-	18,030
Debts of securities company		176	-	-	-	-	-	-	-	-	-	176
Debts of corporations	-	519	-	-	839	-	177,846	3,687	-	-	-	182,891
Debts collateralized by commercial real estate	-	-	-	-	-	-	22,325	555	-	-	-	22,880
Retail exposures to individuals	-	-	-	-	-	63,025	211	210	-	-	-	63,446
Loans to small businesses	-	-	-	-	-	19,521	139	206	-	-	-	19,866
Housing mortgages	-	-	39,275	-	5,550	24,763	5,723	223	-	-	-	75,534
Securitization	-	1,291	-	321	305	-	224	-	30	-	-	2,171
Other assets	2,056	-	-	-	-	-	13,219	449	-	-	-	15,724
Total	69,844	22,593	39,275	321	16,095	107,309	220,952	5,331	30	-	-	481,750

(1) Before conversion to credit of off balance sheet components as required by the Basel II directives (e.g. weighting of unutilized facilities) and before mitigation of credit risk as the result of certain activities (e.g. use of guarantees).

(2) The mitigation of credit risk expresses classification of the final risk weighting between the various rates.

The above comments relate to the tables below.

Amount of exposure after expenses in respect of credit losses, and before mitigation of credit risk (2):

	31 December 2013											
	0%	20%	35%	40%	50%	75%	100%	150%	225%	650%	Deduction from equity	Gross credit exposure (1)
	NIS millions											
Sovereign debts	**67,073**	**2,183**	**-**	**-**	**359**	**-**	**297**	**-**	**-**	**-**	**-**	**69,912**
Debts of public-sector entities	**-**	**5,212**	**-**	**-**	**5,906**	**-**	**-**	**1**	**-**	**-**	**-**	**11,119**
Debts of banking corporations	**715**	**13,208**	**-**	**-**	**3,134**	**-**	**966**	**-**	**-**	**-**	**-**	**18,023**
Debts of securities company		**176**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**176**
Debts of corporations	**-**	**519**	**-**	**-**	**839**	**-**	**175,514**	**3,565**	**-**	**-**	**-**	**180,437**
Debts collateralized by commercial real estate	**-**	**-**	**-**	**-**	**-**	**-**	**22,204**	**514**	**-**	**-**	**-**	**22,718**
Retail exposures to individuals	**-**	**-**	**-**	**-**	**-**	**62,658**	**126**	**207**	**-**	**-**	**-**	**62,991**
Loans to small businesses	**-**	**-**	**-**	**-**	**-**	**19,294**	**55**	**205**	**-**	**-**	**-**	**19,554**
Housing mortgages	**-**	**-**	**39,136**	**-**	**5,529**	**24,706**	**5,470**	**214**	**-**	**-**	**-**	**75,055**
Securitization	**-**	**1,291**	**-**	**321**	**305**	**-**	**224**	**-**	**30**	**-**	**-**	**2,171**
Other assets	**2,056**	**-**	**-**	**-**	**-**	**-**	**13,219**	**449**	**-**	**-**	**-**	**15,724**
Total	**69,844**	**22,589**	**39,136**	**321**	**16,072**	**106,658**	**218,075**	**5,155**	**30**	**-**	**-**	**477,880**

Amount of exposure after expenses in respect of credit losses, and after mitigation of credit risk(2):

	31 December 2013											
	0%	20%	35%	40%	50%	75%	100%	150%	225%	650%	Deduction from equity	Net credit exposure (1)
	NIS millions											
Sovereign debts	**73,326**	**2,205**	**-**	**-**	**359**	**-**	**217**	**-**	**-**	**-**	**-**	**76,107**
Debts of public-sector entities	**533**	**2,302**	**-**	**-**	**3,628**	**-**	**-**	**1**	**-**	**-**	**-**	**6,464**
Debts of banking corporations	**715**	**11,284**	**-**	**-**	**3,044**	**-**	**892**	**-**	**-**	**-**	**-**	**15,935**
Debts of securities company		**176**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**176**
Debts of corporations	**-**	**519**	**-**	**-**	**839**	**-**	**161,470**	**3,499**	**-**	**-**	**-**	**166,327**
Debts collateralized by commercial real estate	**-**	**-**	**-**	**-**	**-**	**-**	**21,321**	**514**	**-**	**-**	**-**	**21,835**
Retail exposures to individuals	**-**	**-**	**-**	**-**	**-**	**60,389**	**107**	**204**	**-**	**-**	**-**	**60,700**
Loans to small businesses	**-**	**-**	**-**	**-**	**-**	**16,842**	**48**	**195**	**-**	**-**	**-**	**17,085**
Housing mortgages	**-**	**-**	**39,130**	**-**	**5,527**	**24,615**	**5,469**	**214**	**-**	**-**	**-**	**74,955**
Securitization	**-**	**1,291**	**-**	**321**	**305**	**-**	**224**	**-**	**30**	**-**	**-**	**2,171**
Other assets	**2,056**	**-**	**-**	**-**	**-**	**-**	**13,219**	**449**	**-**	**-**	**-**	**15,724**
Total	**76,630**	**17,777**	**39,130**	**321**	**13,072**	**101,846**	**202,967**	**5,076**	**30**	**-**	**-**	**457,479**

Amount of exposure before expenses in respect of credit losses, and before mitigation of credit risk (2):

	31 December 2012											
	0%	20%	35%	40%	50%	75%	100%	150%	225%	650%	Deduction from equity	Gross credit exposure (1)
	NIS millions											
Sovereign debts	69,264	2,623	-	-	507	-	276	-	-	-	-	72,670
Debts of public-sector entities	-	3,378	-	-	3,491	-	1,659	1	-	-	-	8,529
Debts of banking corporations	20	14,539	-	-	3,012	-	839	-	-	-	-	18,410
Debts of corporations	-	498	-	-	1,261	-	186,483	4,500	-	-	-	192,742
Debts collateralized by commercial real estate	-	-	-	-	-	-	24,430	806	-	-	-	25,236
Retail exposures to individuals	-	-	-	-	-	57,670	168	185	-	-	-	58,023
Loans to small businesses	-	-	-	-	-	17,655	124	183	-	-	-	17,962
Housing mortgages	-	-	43,337	-	-	18,303	6,758	219	-	-	-	68,617
Securitization	-	727	-	390	169	-	370	-	42	2	21	1,721
Other assets	2,190	-	-	-	-	-	12,899	441	-	-	-	15,530
Total	71,474	21,765	43,337	390	8,440	93,628	234,006	6,335	42	2	21	479,440

(1) Before conversion to credit of off balance sheet components as required by the Basel II directives (e.g. weighting of unutilized facilities) and before mitigation of credit risk as the result of certain activities (e.g. use of guarantees).
(2) The mitigation of credit risk expresses classification of the final risk weighting between the various rates.

The above comments relate to the tables below.

Amount of exposure after expenses in respect of credit losses, and before mitigation of credit risk (2):

	31 December 2012											
	0%	20%	35%	40%	50%	75%	100%	150%	225%	650%	Deduction from equity	Gross credit exposure(1)
	NIS millions											
Sovereign debts	69,263	2,623	-	-	507	-	276	-	-	-	-	72,669
Debts of public-sector entities	-	3,378	-	-	3,489	-	1,659	1	-	-	-	8,529
Debts of banking corporations	20	14,539	-	-	3,012	-	839	-	-	-	-	18,407
Debts of corporations	-	498	-	-	1,261	-	183,638	4,412	-	-	-	189,809
Debts collateralized by commercial real estate	-	-	-	-	-	-	24,348	787	-	-	-	25,135
Retail exposures to individuals	-	-	-	-	-	57,333	116	182	-	-	-	57,631
Loans to small businesses	-	-	-	-	-	17,475	55	181	-	-	-	17,711
Housing mortgages	-	-	43,235	-	-	18,256	6,473	201	-	-	-	68,165
Securitization	-	727	-	390	169	-	370	-	42	2	21	1,721
Other assets	2,190	-	-	-	-	-	12,899	441	-	-	-	15,530
Total	71,473	21,765	43,235	390	8,435	93,064	230,673	6,205	42	2	21	475,305

Amount of exposure after expenses in respect of credit losses, and after mitigation of credit risk (2):

	31 December 2012											
	0%	20%	35%	40%	50%	75%	100%	150%	225%	650%	Deduction from equity	Net credit exposure (1)
	NIS millions											
Sovereign debts	73,194	2,623	-	-	506	-	230	-	-	-	-	76,553
Debts of public-sector entities	499	1,386	-	-	3,482	-	190	1	-	-	-	5,558
Debts of banking corporations	20	13,578	-	-	3,077	-	773	-	-	-	-	17,448
Debts of corporations	-	498	-	-	1,261	-	171,866	4,302	-	-	-	177,927
Debts collateralized by commercial real estate	-	-	-	-	-	-	23,234	786	-	-	-	24,020
Retail exposures to individuals	-	-	-	-	-	55,026	107	179	-	-	-	55,312
Loans to small businesses	-	-	-	-	-	15,146	53	172	-	-	-	15,371
Housing mortgages	-	-	43,232	-	-	18,160	6,470	201	-	-	-	68,063
Securitization	-	727	-	390	169	-	370	-	42	2	21	1,721
Other assets	2,190	-	-	-	-	-	12,899	441	-	-	-	15,530
Total	75,903	18,812	43,232	390	8,495	88,332	216,192	6,082	42	2	21	457,503

Credit risk mitigation

Policy and processes regarding valuation and the management of collateral

As a policy, the Bank aims to give credit against collateral. The amount of collateral required from a borrower derives, inter alia, from the level of risk in the credit. Collateral received is not the principal consideration in approving credit, but rather additional support, intended to minimize the loss to the Bank in the event of the business/financial failure of the borrower.

Within the context of the collateral policy for all sectors of the economy, the Bank has set principles and rules concerning types and amounts of collateral. Requirements and rates of collateral derive from the level of risk that the Bank is willing to assume when providing credit, but special attention is given to risk rating of the borrowers themselves which is determined, taking into account a large number of parameters, the main ones being, financial strength, repayment ability, the sector of industry in which the activity is concentrated

Furthermore, business criteria have been determined for the receipt of collateral, the manner of establishing the rate of reliance on the collateral, courses of action when receiving them, methods and timing for updating their value and the means of control and review, and these are distributed through working procedures, circulars, and operating instructions.

Collateral is matched to the kind of credit that it secures, taking into account the length of the period, types of linkage, the nature of the credit and its purpose, as well as the time frame within which the collateral can be realized. The Bank customarily verifies the value of collateral by obtaining up-to-date appraisals/valuations. Appraisals must be independent and addressed to the Bank.

The Credit Risk Management Unit in the area of real-estate in the Risk Management Division is responsible for the operation of the Appraisal Section whose function, inter alia, is appraisals of real estate assets pledged to the Bank (in excess is the defined threshold amount).

In special transactions, and in cases when shares of a corporation serve as the main collateral and/or the main source of repayment of a loan, an updated appraisal and an examination of the ability of the corporation as a source of debt repayment is required. The appraisal is carried out by one of several generally accepted methods in the Bank, taking into account the circumstances of the matter, such as the description of the corporation, and the economic sector and economic environment in which the acquired corporation operates. Appraisals can be carried out by an expert unit in the Bank or by an external appraiser from the list of appraisers authorized from time to time by the Bank. If the appraisal is carried out by an external appraiser, an audit review will be carried out on it by the business personnel and expert units in the Bank.

The Bank has a computerized system enabling information to be produced about types of collateral. Instructions have been issued concerning the various types of collateral, managing them, determining their value (using external appraisers, financial data, etc.), handling the receipt of collateral, and monitoring changes in collateral and in its value. Officers authorized to approve the credit operate in accordance with prescribed policy. Rates of collateral are calculated automatically by the computerized system according to prescribed policy.

The principles on which collateral reliance rates are determined derive from the degree of liquidity and negotiability of the collateral, ways of realizing the collateral and the speed of realization, the degree of volatility in the value of the collateral, the appraisal of the collateral (internal or external), the degree of control, review and supervision the Bank has over the collateral, the suitability of the type of collateral to the type of financing, and the dependence of the value of the collateral on the condition of the customer.

Special emphases regarding specific collaterals also appear in the Bank's Credit and Credit Risks Policy document.

Common types of collateral accepted by the Bank for the purpose of reducing risks deriving from the grant of credit

- Pledge/offset of monies in accounts held at the Bank or with external entities (shekel/foreign currency deposits, savings, securities, provident funds);
- Pledge of sources for repayment into an account with the Bank (deferred receivables, credit card vouchers, direct debits, open accounts);
- Bank guarantees from banks in Israel and abroad/sovereign guarantees/retention of inter-branch collateral;
- Third-party guarantees;
- Foreign trade risk insurance policies;
- Real estate;
- Floating liens;
- Movable property (vehicles, equipment);
- Pledge and assignment of rights by way of charge (pledges of contract/factoring).

Mitigation of credit risk (Table 7– Basel II):

	31 December 2013					
	Gross credit exposure before allowance for credit losses	Gross credit exposure after allowance for credit losses	Total exposure covered by guarantees deducted	Total amounts added	Total exposure covered by eligible financial collateral	Net credit exposure
	NIS millions					
Sovereign debts	**69,912**	**69,912**	**(79)**	**6,275**	**(1)**	**76,107**
Debts of public-sector entities	**11,120**	**11,119**	**(5,183)**	**533**	**(5)**	**6,464**
Debts of banking corporations	**18,030**	**18,023**	**(1,390)**	**355**	**(1,053)**	**15,935**
Debts of securities company	**176**	**176**	**-**	**-**	**-**	**176**
Debts of corporations	**182,891**	**180,437**	**(486)**	**-**	**(13,624)**	**166,327**
Debts collateralized by commercial real estate	**22,880**	**22,718**	**(5)**	**-**	**(878)**	**21,835**
Retail exposures to individuals	**63,446**	**62,991**	**(4)**	**-**	**(2,287)**	**60,700**
Loans to small businesses	**19,866**	**19,554**	**(14)**	**-**	**(2,455)**	**17,085**
Housing mortgages	**75,534**	**75,055**	**(2)**	**-**	**(98)**	**74,955**
Securitization	**2,171**	**2,171**	**-**	**-**	**-**	**2,171**
Other assets	**15,724**	**15,724**	**-**	**-**	**-**	**15,724**
Total	**481,750**	**477,880**	**(7,163)**	**7,163**	**(20,401)**	**457,479**

	31 December 2012					
	Gross credit exposure before allowance for credit losses	Gross credit exposure after allowance for credit losses	Total exposure covered by guarantees deducted	Total amounts added	Total exposure covered by eligible financial collateral	Net credit exposure
	NIS millions					
Sovereign debts	72,670	72,669	(45)	3,929	-	76,553
Debts of public-sector entities	8,529	8,527	(3,460)	499	(8)	5,558
Debts of banking corporations	18,410	18,407	(927)	496	(528)	17,448
Debts of corporations	192,742	189,809	(426)	-	(11,456)	177,927
Debts collateralized by commercial real estate	25,236	25,135	(37)	-	(1,078)	24,020
Retail exposures to individuals	58,023	57,631	(5)	-	(2,314)	55,312
Loans to small businesses	17,962	17,711	(24)	-	(2,316)	15,371
Housing mortgages	68,617	68,165	-	-	(102)	68,063
Securitization	1,721	1,721	-	-	-	1,721
Other assets	15,530	15,530	-	-	-	15,530
Total	479,440	475,305	(4,924)	4,924	(17,802)	457,503

Activity in Derivative Instruments for the purpose of reducing credit risks

Hedging and/or Risk Mitigation Policy and Strategies and Processes for Monitoring the Continuing Efficacy of Risk-Reducing Hedging Activities

Developments in international foreign currency markets and the volatility of exchange rates of the various currencies, with their implications on those borrowers active in foreign currency, make it necessary to increase activity in monitoring, supervising and controlling customers' exposures to fluctuations in market prices (exchange rate, inflation, etc.). To this end, there are instructions addressing the matching required between the currency basis of the credit and the currency of the cash flow that constitutes the source of repayment of the credit. There is awareness of exposure to currency risks and special attention has been drawn to borrowers with the potential for a high degree of exposure. When necessary, the borrower’s risk rating is revised and a requirement issued to strengthen shareholders' equity and collateral. This area was also tightened up in the Bank's credit policy.

If it appears that a borrower faces exposure/sensitivity to changes in exchange rates and/or commodity prices, the relevant corporate officer must examine the degree of the borrower’s sensitivity from an overall perspective. This examination takes into account all the criteria that require the borrower to be included in the list of sensitive customers, and consideration and quantification of the borrower's sensitivity to changes in exchange rates and/or commodity prices included in its activity.

For the purpose of hedging various credit risks, the Bank recommends its customers make use of defensive mechanisms against macro-economic variables, such as the Consumer Price Index, exchange rates and commodity prices. In order to reduce the level of credit risk, the Bank suggests the borrower protect himself against sharp changes in exchange rates, *inter alia*, by the use of financial instruments. By means of these instruments, it is possible to "hedge" financial exposure and, to a certain extent, real exposure, thus keeping risk to a minimum.

When a solution is not found to fully cover exposure to changes in exchange rates, the Bank examines the need for taking other measures to reduce exposure, such as changing the terms of the loan, increasing collateral requirements, and reducing the borrower's *obligo*, as well as cancelling facilities that have not yet been utilized.

Various exit clauses are included in the credit documents which enable the Bank to discontinue providing credit in foreign currency and to replace it with credit in shekels.

Due to the high volatility of worldwide prices of commodities, special attention is also paid to sectors that are likely to be adversely affected by this trend.

Below are credit risk balances to counterparties in derivatives (Table 8 – Basel II):

	31 December 2013		31 December 2012	
	Par value balance	Net credit exposure of derivatives	Par value balance	Net credit exposure of derivatives
	NIS millions			
Interest contracts	**336,427**	**10,584**	290,808	10,363
Foreign currency contracts	**196,967**	**6,830**	180,438	5,501
Contracts in respect of shares	**63,150**	**3,449**	38,415	2,163
Commodities and other contracts	**6,937**	**293**	1,535	109
Credit derivative transactions (1)	**-**	**-**	187	3
Offset benefits (2)	**-**	**(13,040)**	-	(11,743)
Eligible collateral	**-**	**(2,603)**	-	(1,297)
Total	**603,481**	**5,513**	511,383	5,099

(1) At the date of this report, there are no credit risk exposures in respect of hedging, sold or purchased.
(2) From 31 December 2011, credit risk in respect of derivatives is calculated in accordance with Proper Conduct of Banking Business Regulation no. 313, and is offset against transactions for derivatives with offset agreements.

The par value of a transaction in derivatives does not reflect the credit risk of the transaction. Credit risk is measured by the amount of the maximum loss, according to scenarios that the Bank may incur if the counterparty to the transaction does not comply with the terms of the transaction, after deducting enforceable set-off agreements.

The credit risk at a specified date is defined as the total loss or profit that has arisen from the transaction as at that date, plus the potential risk of additional future loss, this potential being estimated according to the level of expected volatility of the underlying asset and the duration of the remaining period until final settlement of the transaction.

Customer activity in transactions in the various types of derivatives is monitored by the Derivatives Risk Management Department in the Bank’s Capital Markets Division. This department is responsible for the models for calculating the collateral requirement, the parameters used in the models, the computer systems which measure compliance with the frameworks of the activity, work procedures at the branches, and the legal forms that customers sign. In addition, a control overview is carried out in relation to all the customers, while, with respect to a number of customers who work according to complex strategies or in new types of activities not yet computerized, the collateral requirement is directly monitored against the actual activity and collateral frameworks.

Application of the Financial Assets Agreements Law (Netting) enables all future transactions between the Bank and the customer to be considered as a single transaction. This law enables payments to be offset in respect of futures transactions by affixing a single sum, should the customer become subject to insolvency proceedings. Accordingly, the legal forms have been amended and most of the customers have signed the forms.

The following table presents the exposures pertaining to counterparty credit risk:

	31 December 2013	31 December 2012
	NIS millions	
Derivatives hedging a positive gross fair value	**73**	31
ALM derivatives with a positive gross fair value	**12,981**	11,405
Other derivatives with a positive gross fair value	**-**	-
Credit derivatives with a positive gross fair value	**-**	2
Total fair value	**13,054**	11,438

The following table shows credit exposure with respect to the fair value of derivatives, according to counterparties to the contract (reported under other assets), as at 31 December 2013, in NIS millions:

	AAA to AA-	A+	A	A-	BBB to BBB-	BB+ to B-	Unrated	Total
Foreign banks				NIS millions				
Euro zone[(1)]	**2,949**	**-**	**-**	**-**	**-**	**-**	**-**	**2,949**
United Kingdom [(2)]	**1,272**	**-**	**-**	**-**	**-**	**-**	**-**	**1,272**
United States	**1,715**	**-**	**-**	**-**	**-**	**-**	**-**	**1,715**
Other	**340**	**-**	**-**	**-**	**-**	**-**	**-**	**340**
Total foreign banks	**6,276**	**-**	**-**	**-**	**-**	**-**	**-**	**6,276**
Israeli banks [(3)]	**-**	**2,531**	**-**	**-**	**-**	**-**	**-**	**2,531**

Corporate customers, according to sectors of the economy	
Financial services[(4)]	**3,554**
Industry[(5)]	**431**
Construction and real estate	**82**
Transportation and storage	**6**
Trade	**92**
Electricity and water	**4**
Business services	**13**
Private individuals	**19**
Communications and computer services	**19**
Others	**27**
Total corporate customers	**4,247**
Others	**-**
Total exposure	**13,054**

See comments on following page:

The following table shows credit exposure with respect to the fair value of derivatives, according to counterparties to the contract, as at 31 December 2012, in NIS millions:

	AAA to AA-	A+	A	A-	BBB to BBB-	BB+ to B-	Unrated	Total
Foreign banks				NIS millions				
Euro zone(1)	2,172	-	-	-	-	-	-	2,172
United Kingdom (2)	1,262	-	-	-	-	-	-	1,262
United States	2,144	-	-	-	-	-	-	2,144
Other	334	-	-	-	-	-	-	334
Total foreign banks	5,912	-	-	-	-	-	-	5,912
Israeli banks (3)	-	2,031	-	-	-	-	-	2,031

Corporate customers, according to sectors of the economy	
Financial services(4)	2,464
Industry(5)	698
Construction and real estate	105
Transportation and storage	22
Trade	95
Electricity and water	11
Business services	21
Private individuals	14
Communications and computer services	40
Others	25
Total corporate customers	3,495
Others	-
Total exposure	11,438

(1) This amount includes transactions in 5 countries (2012 – includes transactions in 4 countries).
(2) This amount includes transactions with 10 banks (2012 – includes transactions with 11 banks).
(3) This amount includes transactions with 9 banks (2012 – includes transactions with 9 banks).
(4) This amount includes transactions with 413 customers, where the highest amount for a single customer is NIS 763 million (in 2012 – includes transactions with 373 customers, with the customer with the highest amount being NIS 580 million).
(5) This amount includes transactions with 254 customers, where the highest amount for a single customer is NIS 237 million (in 2012 – includes transactions with 260 customers, with the customer with the highest amount being NIS 453 million).

.

Credit concentration

Concentration risk is defined as a single exposure or group of exposures with a common denominator and a potential for causing significant losses. Concentration risk management is conducted by determining restrictions and monitoring and controlling compliance therewith. The aspect of concentration is also reflected in the pricing of credit which reflects the risk.

Dispersal of the credit portfolio among the various sectors of the economy:

The Bank's credit portfolio is split among the various sectors of the economy with the aim of dispersing the risk inherent in the high state of concentration in one sector. In sectors of the economy characterized by a relatively low level of risk, we endeavor to reach a high state of financing from our share in the system.

In addition to the sector dispersal limitation, which was decided by the Bank of Israel with regard to the 20 most important sectors of the market, the Bank defines internal restrictions as a part of its risk policy to disperse the credit portfolio on the basis of the sectors of the economy and the sub-sectors, both as a percentage of the regulatory capital and as a percentage of the credit risk.

Activity and risk restrictions in the construction and real estate sector

This involves the area of activity with the largest exposure of all sectors of the economy. As with other sectors of the economy, restrictions at sector level and sub-sector level are defined for the real estate sector as part of the credit and credit risk policy, and the methodology and parameters for financing transactions are also defined.

In addition, the emphasis given by Leumi to financing real estate is reflected in the fact that a significant part of the Bank's activity in the sector is concentrated in a separate system which is specially adapted for dealing with customers in this area.

The Bank has a special unit to handle complex transactions for financing investments in infrastructure projects (power stations, desalination facilities, toll roads, BOT (Build-Operate-Transfer) projects and the like). This unit examines the transactions and sets up the financing package, including possible cooperation with capital market entities in financing the transaction.

The real estate sector is financed, ensuring a diversification of the credit portfolio, distinguishing between the various segments – initiation of housing construction, building contracting including performance contracting, infrastructure works, activities in non-housing real estate – income-yielding assets, building products industry, trade in building products, and geographical areas in which the projects are located according to the relevant demands.

A significant part of the financing of the construction is carried out in the "closed project" (construction loan) format, which is characterized by periodic examination and close monitoring, while relying on and with the assistance of external building supervisors.

As a part of the Bank's strategy to finance its customers in all the places in which they operate, and with a tendency to disperse risks, the Bank also regularly participates in the financing of real estate abroad. The financing is effected for customers on a selective basis, with whom the Bank has positive experience, in a controlled fashion and after examining all their activity in Israel and abroad, in preferred countries and taking into consideration the country's political and economic risk, with a meticulous examination of the projects, with the Bank's overseas units overseeing the projects.

Group of borrowers[1]

The Bank monitors the exposure of groups of borrowers in all their components, using the mechanized system that serves the Bank for the purposes of regular reporting to the Bank of Israel and for internal monitoring and examination of compliance of the scope of obligation of groups of borrowers with the regulatory limitations. In addition, there is an internal process, in the framework of which a central official ("the Group head") is appointed for each of the large groups and there is coordination and information flow regarding the group components with the objective of reinforcing, as much as possible, the control on credit exposure and concentration risk deriving therefrom. This process occurs between the various units in Leumi and also includes the subsidiaries, and obliges the business entities involved with management of groups of borrowers to provide constant flow of information relating to the requests made for credit and the ratio of risk to Group items, exercising discretion regarding the scope of information and entities to whom it is transferred.

Moreover, regarding the largest 10 groups of borrowers, the head of the group dealing with these groups, is required, once a year, to provide the Board of Directors of the Bank with a comprehensive review of the group.

With regard to the management of the credit portfolio of the Bank as a whole, the Bank implements an internal process of estimating concentration risk inherent in the exposure to all the large groups of borrowers, and the effect of that risk on the overall risk level of the portfolio. The above process enables both the quantification of the allocation of adequate equity according to the Proper Conduct of Banking Business Directive, and the performance of follow-up and ongoing monitoring of trends within the concentration component as part of the development trends of the entire portfolio.

The regulatory limits on the indebtedness of a group of borrowers, as set forth in Proper Conduct of Banking Business Management Regulation no 313, are as follows:

1. The net indebtedness of a group of borrowers / group of banking borrowers must not exceed 25% of the Bank's capital.

2. The net indebtedness of a controlled group of borrowers must not exceed 50% of the Bank's capital.

3. The net aggregate indebtedness of borrowers / groups of borrowers/groups of banking borrowers, whose net indebtedness exceeds 10% of the Bank's capital, must not exceed 120% of the Bank's capital.

As of 31 December 2013, the Bank complies with these limits.

For information regarding credit to groups of borrowers whose indebtedness exceeds 15% of the equity of the Bank, see above in chapter, "Structure and Development of Assets and Liabilities".

Exposure of the Bank to leveraged finance

Proper Conduct of Banking Business Directive 311 provides that a bank's credit policy should relate to leveraged finance. The Bank operates according to a unique credit policy for the area. It should be noted that there is no banking directive specifically for leveraged financing. The leveraged credit data is presented in this report for the first time.

1 A group of borrowers is defined as all the following together: the borrower, a person controlling it or anyone controlled thereby. When a corporation is controlled by more than one individual, it is required to include in one group of borrowers those controllers for which the controlled corporation is material (e.g., from a capital perspective), including the controlled corporation and anyone controlled by them; an investee corporation which is material for a holder who has no control and anyone controlled by them; borrowers related in such a way that the impairment in the financial stability of any of them is likely to have implications for the financial stability of the other, or that those factors are likely to have implications for the financial stability of both of them.

The Bank defines leveraged finance as finance that meets one of the following criteria:

1. Financing the purchase of the means of control held (constitutes an expansion to that required pursuant to Proper Conduct of Banking Business Directive 323). See also separate consideration below.

2. Financing purely holding companies, as defined in the Bank's policy.

3. Financing a borrower in the various segments of the defined industry sectors, characterized in significant exceptional values of certain parameters in relation to norms in the area of the relevant market sector, such as the ability to service an insufficient debt compared to norms established by the Bank, a low shareholders' equity to total assets ratio.

The following table presents the aggregate balances of credit to leveraged borrowers, each of which has the balance of credit amounting to 0.5% of the Bank's capital, by sector of the economy, as of 31 December 2013:

Economic sector	Balance sheet and off-balance sheet credit, net*
	NIS millions
Industry	**2,868**
Trade	**666**
Transport and storage	**224**
Real estate	**2,629**
Communications	**308**
Financial services	**1,512**
Other corporate services	**331**
Total	**8,538**

(*) Net of allowances of credit losses and deductible collateral (and including the holding of debentures in nostro and irrevocable undertakings to grant credit).

In addition, the Bank has established internal quantitative limits relating to leveraged financing, both absolutely and in relation to the Banks capital ratio.

The Bank has decided that reports will be presented to the Board of Directors and Bank management every six months on the compliance with the quantitative limits that have been established and on the volume of the portfolio, including trends and changes.

Exposure limits in transactions to finance the means of control

Credit for acquiring the means of control is defined in Proper Conduct of Banking Business Regulation no. 323.

The regulation applies to transactions that fulfill the following two conditions, in aggregate:

a. The credit balance is higher than 0.5% of the Bank's capital.

b. The repayment of the credit is mainly based on the acquired corporation.

The regulation provides quantitative limits on the balance of credit for acquiring the means of control, and the Bank complies with them.

In addition, the Bank has established additional internal limits in the quantitative plain and the qualitative plain, relating both to transactions for acquiring the means of control according to the regulation and to transactions for any purpose against the means of control.

The following table presents the balances of credit for financing the purchase of the means of control* pursuant to Proper Conduct of Banking Business Management Regulation no. 323 by industry sector:

	Balance sheet and off balance sheet credit **	
	31 December 2013	31 December 2012
Economic sector	NIS millions	
Industry	**1,437**	1,901
Trade	**263**	717
Real estate	**406**	511
Communications	**308**	547
Total	**2,414**	3,676

* The credit balances according to Regulation 323 constitutes a part of the balances of leveraged finance which is set forth above.

** Net of credit loss allowances and deductible collateral

As of 31 December 2013, the Bank complies with the limits.

Geographic dispersal

Mapping of exposure data of the activity of borrowers to countries/regions:

Geographic dispersal is defined as one of the credit concentration risks in a portfolio (in addition to sector dispersal and exposure to large borrowers and to groups of borrowers). Geographic dispersal means: Economic/political/security deterioration in countries to which the borrower is exposed is likely to lead to impairment in the financial position of the company and its ability to meet its liabilities.

In 2009, questions relating to geographic exposure were added in the system of borrower rating questionnaires. This referred to the mix of revenues and/or the mix of the firm's cash flows, the location of the material assets being used and creating its activity (assets used in generating revenue, such as plant, logistical center, warehouse, head offices, rental property, etc.), as well as assets used as collateral for the company's debts.

These data enable the Bank to conduct an examination from the perspective of the entire portfolio of the exposure of the borrowers to the various countries, for the purposes of monitoring and risk management.

Credit exposure to foreign financial institutions

The following table sets out the credit exposure to overseas financial institutions [(1)]:

	As at 31 December 2013			
	Balance sheet credit risk [(2)]	Securities [(3)]	Current off-balance sheet credit risk [(4)]	Current credit exposure [(6)]
	NIS millions			
External credit rating[(5)]				
AAA to AA-	**13,469**	**1,074**	**4,275**	**18,818**
A+ to A-	**1,752**	**32**	**125**	**1,909**
BBB+ to BBB-	**171**	**190**	**917**	**1,278**
BB+ to B-	**80**	**1**	**79**	**160**
Below B-	**1**	**-**	**-**	**1**
Unrated	**142**	**-**	**-**	**142**
Total current credit exposure to overseas financial institutions	**15,615**	**1,297**	**5,396**	**22,308**
Problem debt balances	**-**	**-**	**-**	**-**

	As at 31 December 2012			
	Balance sheet credit risk [(2)]	Securities [(3)]	Current off-balance sheet credit risk [(4)]	Current credit exposure [(6)]
	NIS millions			
External credit rating [(5)]				
AAA to AA–	14,921	3,746	1,119	19,786
A+ to A–	669	406	-	1,075
BBB+ to BBB-	147	1,140	205	1,492
BB+ to B–	126	77	23	226
Below B-	-	-	16	16
Unrated	-	-	2	2
Total current credit exposure to foreign financial institutions	15,863	5,369	1,365	22,597
Problem debt balances	5	-	-	5

(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 amounting to NIS 998 million as at 31 December 2013 and NIS 1,272 million as at 31 December 2012.
(4) Mainly guarantees and undertakings for the provision of credit (excluding off-balance sheet derivatives).
(5) The bank only uses the rating of Moody's and S&P credit rating agencies to rate the foreign financial institutions to which there is a credit exposure.
(6) Credit exposure is presented after deduction of the specific allowances for doubtful debts.

Notes:

a. Credit exposures do not include investments in asset-backed securities. (See the details in the note on securities.)
b. Some of the banks have received government support of various types, including direct investment in the Bank's capital, government guarantees of certain asset portfolios of the banks, guarantees enabling the banks to raise sources of financing, etc.
c. 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 18 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 44%, Europe (Germany, France, Italy, Spain and the Benelux countries) 23%, United Kingdom 23%, and other countries, 10%.

The exposure includes mainly deposits in overseas banks for short periods of up to one week, and debentures, usually for a period of up to five years. The Bank closely monitors the condition of banks worldwide, and makes frequent analyses of their financial stability. The Bank maintains a shortlist of quality banks with which the Bank and its overseas subsidiaries make deposits.

For additional details regarding investments in securities, mainly debentures of foreign banks, are presented above, see above in chapter, "Structure and Development of Assets and Liabilities - Securities".

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

- Their size as reflected, *inter alia*, in the size of their shareholders' equity.
- Their strength, as reflected in capital adequacy ratios (especially Tier 1 capital), analysis of the quality of their assets, and the stability of their profitability.
- 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 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 per risk.

Exposure to foreign countries [1]:

The exposure to foreign countries 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 (Table 4(c) – Basel II):

	31 December 2013		
	Balance sheet credit risk	Off-balance sheet credit risk (2)	Total credit risk
	NIS millions		
USA	**26,360**	**9,243**	**35,603**
UK	**12,956**	**5,543**	**18,499**
France	**2,796**	**1,923**	**4,719**
Germany	**5,045**	**1,028**	**6,073**
Switzerland	**2,910**	**773**	**3,683**
Belgium	**700**	**183**	**883**
Italy	**328**	**35**	**363**
The Netherlands	**2,380**	**139**	**2,519**
Denmark	**582**	**14**	**596**
Norway	**46**	**0**	**46**
Austria	**83**	**13**	**96**
Sweden	**139**	**18**	**157**
China	**567**	**548**	**1,115**
Others	**5,673**	**866**	**6,539**
Total	**60,565**	**20,326**	**80,891**

	31 December 2012		
	Balance sheet credit risk	Off-balance sheet credit risk (2)	Total credit risk
	NIS millions		
USA	25,916	7,391	33,307
UK	11,756	5,041	16,797
France	2,904	1,398	4,302
Germany	4,066	1,030	5,096
Switzerland	3,553	1,021	4,574
Belgium	303	200	503
Italy	348	35	383
The Netherlands	3,063	161	3,224
Denmark	736	41	777
Norway	245	0	245
Austria	72	35	107
Sweden	141	2	143
China	411	202	613
Others	5,380	1,099	6,479
Total	58,894	17,656	76,550

(1) In connection with exposure to foreign countries, see also Exhibit E.

(2) Effective 31 December 2011, credit risk in respect of derivatives is calculated according to Proper Conduct of Banking Business Regulations no. 313 and offset against transactions with offset agreements.

The following table presents the exposure to countries according to the countries' credit rating as rated by the World Bank, in NIS millions, as at 31 December 2013:

Rating	Balance sheet exposure	Off-balance-sheet exposure	Total exposure	Percentage of exposure in relation to total	Of which, classified as problematic
OECD countries with high income	**56,849**	**19,186**	**76,035**	**94**	**1,547**
Countries with high income	**874**	**68**	**942**	**1.2**	**2**
Countries with mid-high income	**2,735**	**905**	**3,640**	**4.5**	**505**
Countries with mid-low income	**101**	**165**	**266**	**0.3**	**3**
Countries with low income	**6**	**2**	**8**	**-**	**-**
Total	**60,565**	**20,326**	**80,891**	**100**	**2,057**

The amount of exposure to countries with liquidity problems as defined by the Fitch liquidity index and by the Bank of Israel (a country receiving monetary assistance from the IMF or whose liabilities are rated with a credit rating of CCC or lower) totals NIS 1,803 million and relates to 13 countries.

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

High income - exceeding US$ 12,616 per capita.
Mid-high income - from US$ 4,086 to US$ 12,615 per capita.
Mid-low income - from US$ 1,036 to US$ 4,085 per capita.
Low income – up to US$ 1,035 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, Israel, Hungary, France, United Kingdom, Japan, Spain, Switzerland, Luxembourg, Slovenia, the Netherlands, Sweden, Poland, Germany and South Korea

b. Countries with high income:

Cyprus, Hong Kong, Monaco, Singapore, Cayman Islands and Croatia

c. Countries with mid-high income:

Argentina, Brazil, Bulgaria, Chile, Mexico, Panama, Romania, Russia, South Africa, Turkey, Venezuela, Uruguay, Columbia and Peru

d. Countries with mid-low income:

China, Ecuador, Egypt, India, Jordan, Paraguay, the Philippines, Thailand and the Ukraine

e. Countries with low income:

Most of the African countries, Haiti and Nepal

Overall exposure to certain foreign countries:

Country	31 December 2013 Credit to the public	Bonds	Bank deposits	Other	Total
	NIS million				
Italy (1)	**64**	**245**	**18**	**36**	**363**
Ireland	**40**	**279**	**-**	**-**	**319**
Greece	**3**	**-**	**-**	**1**	**4**
Spain	**9**	**111**	**-**	**33**	**153**
Total (2)	**116**	**635**	**18**	**70**	**839**

(1) Of which NIS 248 million in Bank Intessa.
(2) The Group has no exposure in respect of Portugal.

Problem debts – disclosure, assessment, classification and rules for credit loss allowance

The Bank follows the instructions of the Supervisor of Banks as of 1 January 2011 in respect of expenses in credit losses and problem debts. The Bank's practice is to estimate, assess and update the amount of the allowance for credit losses for each calendar year, in accordance with economic forecasts, assessments regarding the various markets and past experience.

The allowance for credit losses in relation to the credit portfolio may be divided into an individual allowance and a collective allowance.

The actual rate of allowance for 2013 amounted to NIS 268 million, representing 0.11% of the credit portfolio. The rate is influenced by a number of factors:

- A low rate of individual allowances in light of the lack of allowances in respect of prominent customers.
- The rate of collections similar to 2012.
- A reduction in the rate of collective allowance in light of the changes in the credit mix and credit balances.

For further information and for a table detailing the credit risk and non-performing assets, see above in the chapter, "Development of Income, Expenses and Provision for Tax".

Market and Liquidity Risks

Market risk and other financial risks policy

Market risk is defined as risk of a loss in off-balance sheet positions arising from changes in the fair value of a financial instrument as a result of a change in market conditions (a change in price levels in various markets, fluctuations in interest rates, exchange rate, inflation, the prices of shares and commodities and other economic indices). Exposure to market risks is reflected in the business results, the fair value of assets and liabilities, shareholders’ equity, cash flows and the value of the Bank.

The policy for managing market risks is intended, on the one hand, to support the achievement of business goals by assessing the risks and the damage that can result from exposure to risks, in comparison with the forecast profit from them, and on the other hand, to reduce the level of risk deriving from the Bank's ongoing activity, including maintaining a high liquidity level. All this is after taking into account the volume of activity, limitations, and the costs of hedging activity, the changes occurring in the business environment in Israel and throughout the world, directives and requirements of the Bank of Israel, and developments occurring worldwide with regard to measurements and methods of managing risks and adapting them to the needs of the Group and the Bank.

Exposure to credit risk is routinely managed at the Group level. The overseas subsidiaries determine policy for the management of market risk corresponding to the Group policy and the risk framework approved therein. Information on the actual state of exposure according to the frameworks so determined is received from the subsidiaries and taken into account in the overall management of the Group exposure.

Management of market risks is handled by two main risk centers – the banking portfolio and the trading portfolio. Definition of the trading portfolio is derived from the Basel directives and includes the securities trading portfolio of the Bank and derivative transactions in trading activity. The banking portfolio includes transactions that are not included in the trading portfolio.

Policy for the management of market risk includes restrictions on financial exposure in accordance with the risk appetite (the economic value and the accounting profit). These restrictions are aimed at limiting the damage likely to be caused as a result of unexpected changes in various risk factors existing in the markets. The system of restrictions demarcates the impact of exposure of the economic value, the accounting profit and the liquidity position, to unexpected changes in the various risk factors, such as interest rates, inflation, exchange rates, etc. The restrictions prescribed at the Group level include all subsidiaries in Israel and overseas.

In December 2012, the Board of Directors approved the risk appetite and investment strategy in a general overview of activity in the *nostro* portfolio and non-bank investments. The strategy includes the classification of the products and activities by risk type and determines risk restrictions according to various cutoffs, including a minimum limit on exposure to low-risk products, a maximum limit on exposure to high yield-to-risk products and restrictions on the maximum exposure to specific products. The set of restrictions guarantees a wide distribution from various aspects – the geographical aspect, the aspect of products and specific counterparties. The Risk Management Division and the Capital Market Division regularly examines the classification of products according to the risk levels and updates them as necessary, in order to prevent exceeding the risk restrictions that have been set.

Structure and functions of market risk management

The Bank implements Proper Conduct of Banking Business Directive No. 339 of the Supervisor of Banks, in the matter of the management of the market risks of the Group. The directive sets out basic principles for the manner of managing and controlling risks, including the responsibility of Management and the Board of Directors, the definition of means of control and tools for measuring risk, and the means of control and supervision of these risks, implementing corporate governance, which includes "three lines of defense", as outlined in the introduction to this chapter.

The Risk Management Division, headed by the Chief Risk Officer, independently examines and monitors the extent of the risk and the procedure for managing the risks and prescribes the risk management policy. A chief market risk manager, who reports to the Chief Risk Officer, is appointed with the status of section head.

The Capital Markets Division deals with the Bank's management of nostro and the operation of all the dealing rooms in the Bank for the purpose of trading and brokering in currencies, interest, derivatives and securities. In addition, the Division is engaged in the overall financial management of financial product development and investment products and the management of the Group's assets and liabilities. Further, the Division is responsible for maintaining the relationship with overseas financial institutions and for providing service to customers operating on financial and money markets, including institutional customers and in the day-to-day management of control of risks of all the abovementioned activities.

Market risk management is discussed in the following committees:

- The Risk Management Committee of the Board of Directors – Once every quarter, the Risk Management Committee of the Board of Directors conducts a discussion on exposures to market risks and the change in risk focus points. The committee reports the position regarding compliance with the limits at Group level, and the damage that the Bank might incur from stress scenarios. In addition, any new activity in financial instruments that is significantly different from the current activity in financial instruments is presented for discussion and the approval of the committee within the context of a "new product" procedure. The recommendations of the Board of Directors Risk Management Committee are presented for approval by the Board of Directors in plenum.
- The Upper Risk Management Committee headed by the President and CEO of the Bank – The policies crystallized in the Market Risk Management Committee (below) are presented and approved to the Upper Risk Management Committee headed by the President and CEO, the Chief Risk Manager and all members of the Bank's management. In addition, subjects on market risks that are on the agenda are discussed.
- The Management Committee for Current Matters headed by the President and CEO, which meets every week, reports on the financial exposure position to market and liquidity risks and compliance with the restrictions determined by the Board of Directors. Periodically (every four to six weeks), the President and Chief Executive Officer reports in the context of the CEO's Report to the Board of Directors on exposure to market risks.
- The Risk Management Division's quarterly exposure document is presented to the Board of Directors and the Board's Risk Management Committee each quarter. If necessary, a report on material changes in exposure is transferred more frequently as part of the CEO's report, which is circulated to the Board of Directors once every six weeks.
- The Market Risks Management Committee, headed by the Chief Risk Officer, examines events and market trends which could have repercussions for the Bank, and it is its responsibility to discuss and approve risk policy and restrictions - prior to their being brought for discussion and the approval of the Board of Directors, monitor compliance with the aforementioned restrictions, approve the methodology for measuring exposure and, periodically, check and discuss market risks in the subsidiaries.
- The Assets, Liabilities and Financial Investments Committee (ALCO), headed by the Head of the Capital Markets Division, is responsible for managing the assets and liabilities and financial investments, giving emphasis to the structure of the balance sheet, transfer prices, the required liquidity and liquid reserve investments, capital structure and capital-raising policy.

Quantitative tools for risk management

Market risks are assessed using a wide array of tools, which complement each other and match the Bank's various exposures in the trading rooms, the nostro investment activity and the activity of asset and liability management.

Sensitivity analysis and stress scenarios

Global and domestic markets are sometimes subjected to shocks which are reflected in particularly wild fluctuations of the parameters, deviating from normal historical behavior. Quantitative models, such as the VAR or other models, do not provide information on losses that may be incurred under extreme market conditions, or beyond an established level of significance. Accordingly, a risk measurement is taken under a range of stress market scenarios, and sensitivity analysis for changes in one of the risk factors. These include all of the risk factors to which the Bank is exposed and constitute a part of the decision-making process in determining an overall investment strategy and the desired portfolio composition under the restrictions of the risk appetite established.

Value at Risk (VaR)

The risk measured\ using the VaR, a probability model, refers to the potential loss from holding all positions in currencies, in an index, in interest rates, and in balance sheet and off-balance sheet shares, including the positions of the trading portfolio, which are exposed to changes in market prices. It actually measures the expected fall in the present value of the assets, less the liabilities in the given mix of the capital structure, with a 99% confidence level, and for a position-holding period of two weeks, according to a given statistical breakdown. The calculation is based on the economic value of the capital by discounting assets and liabilities at risk-free interest rates prevailing in the market.

The measurement of the VaR is carried out on the overall risk and on the risk divided into segments (exposure risk on a basis according to currency, exposure on interest according to segments and according to various time periods, shares risk), and, as a result of the coefficients (the dispersal effect) between the various factors, the general VaR is lower than the VaR according to segments.

Model for estimating the (marketable) credit risk in the nostro foreign currency portfolio

The model calculates the expected loss in the foreign currency nostro portfolio in scenarios of varying degrees of severity, based on specific characteristics of the portfolio, taking into account the probability of a failure and change in the ratings of issuers. The measurement of the risk in the entire portfolio is performed taking into account the dispersal and concentrations in the portfolio. The model calculates the expected shortfall, which reflects the potential average loss within a timeframe of a year and a probability of 1%.

Capital requirement in respect of market risk

The capital requirements in respect of market risks (Table 10 – Basel II), as required pursuant to the standardized approach, are presented below. These requirements reflect only a small part of the capital held by Leumi against market risks (First Pillar of the Basel II framework). In addition to this capital, the Group holds additional equity against market risks and nostro activity, in the framework of the Second Pillar of Basel II.

The following table sets forth the capital requirements in respect of market risks (Table 10 – Basel II):

	31 December 2013	31 December 2012
	NIS millions	
Capital requirement in respect of:		
Interest risks	**707**	673
Share price risk	**127**	14
Exchange rate risk	**69**	117
Options	**43**	70
Total capital requirement in respect of market risks	**946**	874

Main focus points in market risks

1. Exposure to interest rates

Risk of a loss as a result of changes in risk-free interest rates of credit in the various currencies, due to differences between the repayment date of the assets and liabilities in each of the linkage segments.

The interest exposure policy restricts the extent of exposure to possible changes in interest on the Bank's profits and on shareholders' equity. Accordingly, in each sector, the exposure to an unexpected change of 1% in interest in all the periods is measured, relating to the potential erosion of economic value[1] and of the accounting profit for the year resulting from a shift in the yield curves in each of the segments and also for all segments together. Exposure of the profit to interest is heavily influenced by the activity remeasured at market prices (derivative transactions and commercial portfolios).

[1] The economic value of the capital is defined as the difference between the current value of assets and liabilities. In calculating present value, cash flows are deducted from the risk-free credit yield curve and the foreign currency LIBOR flows.

There are structured interest risks arising from the uncertainty in the market factors that may be hedged, but are structured in the banking activity. The risk includes gross behavioral options in loans and deposits that may not be hedged (early repayment options, for example).

The interest risk is actually measured and managed on the basis of various behavioral assumptions with regard to the repayment times of the assets and liabilities. The principal assumptions are:

- In the index-linked sector, an estimate is taken into account with regard to breakages and withdrawals at exit points in savings plans. The estimate is derived from past customer behavior.
- In accordance with accumulated experience, there is a long-standing stable credit balance in non-interest bearing current accounts. Accordingly, for purposes of measuring and managing interest rate exposure, Bank policy is to regard part of the non-interest bearing current account balances as a long-term liability. Periodically, the change in the non-interest bearing current account balances is examined in order to decide how it should be spread. In view of the low interest rates, the current account spread was changed, with effect from June 2012.
- Leumi Mortgage Bank – The management of exposures takes account of assumptions with regard to early repayment of loans. Assumptions regarding CPI-linked loans at fixed rates of interest rely on a statistical model for predicting early repayments. This statistical model is checked regularly. At the same time, Leumi Mortgage Bank has developed a repayment model including all linkage segments to be assimilated in the management of activity.

The summary of exposures to unexpected changes in interest at Group level (before tax and in NIS millions)* is as follows:

	Potential erosion in economic value		Potential erosion in annual profit	
Effect of immediate parallel change of 1% on the yield curve	**31 December 2013**	31 December 2012	**31 December 2013**	31 December 2012
Actual	**853**	742	**184**	182
Limit	**1,100**	1,100	**500**	500

* The extent of exposure does not take into account the existence of an interest rate floor of 0% on the deposits. The further the interest falls and approximates to zero, the higher the impairment in financial margin.

In 2013, the potential erosion in economic value ranged from NIS 625 million to NIS 1,038 million, and in annual profit, from NIS 125 million to NIS 350 million.

In 2013, the Group complied with all of the exposure restrictions for interest prescribed by the Board of Directors.

Sensitivity of the fair value of assets and liabilities to interest

The effect of potential changes in interest rates on the fair value of the financial instruments of the Bank and its consolidated subsidiaries, except for non-monetary items, according to accounting principles, is as follows:

The net fair value of financial instruments, before the effect of changes in interest rates:

	31 December 2013				
	Israeli currency		Foreign currency, including Israeli currency linked to foreign currency		
	Unlinked	CPI-linked	Dollar	Euro	Others
	NIS millions				
Financial assets	**211,239**	**59,960**	**51,750**	**12,220**	**13,830**
Amounts receivable in respect of derivative financial and off-balance sheet instruments	**311,649**	**7,098**	**116,357**	**41,980**	**23,574**
Financial liabilities	**169,974**	**53,425**	**76,368**	**17,574**	**10,978**
Amounts payable in respect of derivative financial and off-balance sheet instruments	**334,405**	**9,844**	**94,024**	**36,403**	**26,209**
Net fair value of financial instruments	**18,509**	**3,789**	**(2,285)**	**223**	**217**

	31 December 2012				
	Israeli currency		Foreign currency, including Israeli currency linked to foreign currency		
	Unlinked	CPI-linked	Dollar	Euro	Others
	NIS millions				
Financial assets	204,561	62,635	59,575	12,066	14,814
Amounts receivable in respect of derivative financial and off-balance sheet instruments	280,774	5,874	119,103	28,982	26,075
Financial liabilities	168,101	54,421	82,296	17,808	11,425
Amounts payable in respect of derivative financial and off-balance sheet instruments	300,234	12,632	96,660	22,990	29,799
Net fair value of financial instruments	17,000	1,456	(278)	250	(335)

The effect of changes in interest rates on the net fair value* of financial instruments (Table 14 – Basel II):

	31 December 2013						
	Fair value, net, of financial instruments after the effect of changes in interest rates					Change in fair value	
	Israeli currency		Foreign currency, including Israeli currency linked to foreign currency				
	Unlinked	CPI-linked	Dollar	Euro	Others	Total	Total
	NIS millions					NIS millions	%
Immediate corresponding increase of 1%	**17,787**	**3,708**	**(2,472)**	**228**	**202**	**(1,000)**	**4.89**
Immediate corresponding increase of 0.1%	**18,437**	**3,781**	**(2,304)**	**224**	**215**	**(100)**	**(0.49)**
Immediate corresponding decrease of 1%	**19,303**	**3,819**	**(2,044)**	**237**	**224**	**1,086**	**5.31**

	31 December 2012						
	Fair value, net, of financial instruments after the effect of changes in interest rates					Change in fair value	
	Israeli currency		Foreign currency, including Israeli currency linked to foreign currency				
	Unlinked	CPI-linked	Dollar	Euro	Others	Total	Total
	NIS millions					NIS millions	%
Immediate corresponding increase of 1%	16,561	1,546	(387)	239	(346)	(479)	(2.65)
Immediate corresponding increase of 0.1%	16,956	1,465	(290)	249	(336)	(48)	(0.27)
Immediate corresponding decrease of 1%	17,485	1,275	(179)	260	(320)	429	2.37

* Not including estimate of the value of revenues in respect of commission for early repayment.

1.1 Exposure to interest rates and compliance with restrictions

The status of exposure to interest changes at the Group level, which is calculated according to accounting principles, is set forth below. During 2013, the Group complied with all the exposure restrictions for interest set by the Board of Directors. For detailed data on exposure to interest, see below Exhibit D in the Management Review.

	31 December 2013			31 December 2012		
	Unlinked	Index linked	Foreign currency and linked thereto	Unlinked	Index linked	Foreign currency and linked thereto
Average duration of assets (1)	**1.19**	**2.94**	**0.86**	1.04	2.81	0.78
Average duration of liabilities (1)	**1.10**	**3.21**	**0.74**	0.98	3.26	0.70
Duration gap in years	**0.09**	**(0.27)**	**0.12**	0.06	(0.45)	0.08
Internal rate of return (IRR) (%)	**2.58**	**0.76**	**1.54**	1.30	0.86	0.81

(1) Including future transactions and options, and based on fair value data of financial instruments.

In calculating the average duration of the liabilities in the index-linked segment, an estimate regarding early repayments and withdrawals at exit points in the savings programs is taken into account, in accordance with a model which estimates the expected early repayments on the basis of the savers' behavior. An average duration of the total liabilities according to the original cash flow of the savings programs is higher, reaching 3.31 years, and the internal rate of return gap (hereinafter "IRR") amounts to 0.52%.

Early repayments of index-linked mortgage loans are taken into account in the figures set forth above, in accordance with a statistical model, which estimates the expected repayments on the basis of the borrowers' behavior in the past. The average duration of the assets at the end of 2013, according to the original cash flow which does not take into account early repayments, is longer, reaching 3.35 years, and the IRR gap amounts to 0.52%.

Exhibit D in the Management Review presents current account balances according to the Bank of Israel directives on deposits with demand of up to a month. On the other hand, for the purpose of exposure to interest, a certain rate from the current account balances in shekels and foreign currency was spread for repayment periods up to 10 years. This is in accordance with the model of behavior, whose basic assumptions are regularly updated. Taking these assumptions into account, the average duration of the liability is higher, reaching in unlinked shekels, 1.18 years, and in foreign currency, 0.87 years, and the difference in the IRR amounts to 1.93 and 1.08, respectively.

2. Basis exposure

The exposure to basis risk is reflected in the loss which is likely to occur as a result of changes in the consumer price index and in exchange rates, as a result of the difference between the value of assets and liabilities, including the effect of futures transactions, in each of the linkage sectors.

According to accounting principles, capital is defined as an unlinked shekel source. Thus, an investment of capital in a segment other than the unlinked shekel segment is defined as basis exposure. Exposure to basis risk is measured as a percentage of the Group's exposed capital.

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

Exposure limits approved by the Board of Directors are decided in accordance with considerations of expected return and risk and are allocated among the trading rooms, ALM and subsidiary companies.

The subsidiaries abroad and in Israel generally maintain low levels of basis exposures, on the basis of policies which are anchored in resolutions of the Board of Directors, and in coordination with the Bank in Israel.

Changes in the exchange rate affect the effective tax rate, because exchange rate differentials in respect of investments abroad are not taken into account in the income basis for calculating the provision for tax, unlike exchange rate differences in respect of sources of financing, and thus, there is a lack of symmetry with respect to exchange rate differences. In the past, the Bank has carried out hedging transactions against tax exposure. From 2012, the accounting policy for investments in the United States and Switzerland, such that they were defined as units whose functional currency was changed from the shekel, and exchange rate differences in respect of the investments and those in respect of the defining sources are carried to a capital reserve. The Bank decided not to renew the hedging transactions in respect of these companies.

Changes in exchange rates have an effect on current income in foreign currency. Hedging activity was carried out in 2013 against the expected net income.

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

	Approved limits Maximum excess (or deficit)	Actual position **31 December 2013**	31 December 2012
		%	
Unlinked	65% - (65)%	**(10.2)**	(5.2)
CPI-linked	50% - (50)%	**6.4**	3.9
Foreign currency	15% - (15)%	**3.8**	1.3

In 2013, the percentage of capital invested on average over the year in the linked segment was 7%. During the year, the percentage ranged from a surplus of 11% to a deficit of 1% of the exposed capital. Capital was channeled to the foreign currency-linked sector at a relatively low rate, and therefore, the effect of the change in exchange rate on pre-tax profit was not material.

In 2013, the Group complied with all the basis exposure restrictions approved by the Board of Directors.

The following table presents sensitivity to changes in the exchange rate of the main foreign currencies as of 31 December 2013. The measurement relates to the effect of the changes in the Bank's capital and includes activity in balance sheet and off-balance sheet instruments:

	Dollar	Euro	Pound sterling	Swiss franc	Yen
	NIS millions				
Increase of 5% in exchange rate	**16**	**20**	**7**	**3**	**3**
Increase of 10% in exchange rate	**48**	**32**	**17**	**7**	**3**
Decrease of 5% in exchange rate	**(1)**	**(21)**	**(4)**	**(3)**	**(2)**
Decrease of 10% in exchange rate	**(7)**	**(16)**	**(7)**	**(6)**	**(1)**

These data do not take into account the effect of a change in the exchange rate on the flow of income and expenses in foreign currency in respect of which hedging was made in 2013.

3. Exposure in the trading rooms

The market risks in the trading portfolio arise as a result of the Bank's activity as a market-maker and as a manager of nostro positions:

- Market-making activity – The Bank is a leader in the scope of activity in the area of derivatives and provides immediate services to customers active in the instruments. In the foreign currency and derivatives dealing room, market-making activity is carried out at the spot desk (in shekels and in foreign currency), at the options desk (in shekels and foreign currency) and at the interest desk (in shekels and foreign currency). This activity exposes the Bank to market risk (exchange rate risk and interest risk) and accordingly, the activity is managed and monitored in accordance with the restrictions approved by the Market Risk Management Committee. Due to the dynamic nature of the activity, these restrictions are regularly monitored at least once a day by the Middle Office.
- *Nostro* trading activity – In the trading room, there is initiated activity whereby initiated exposures are taken for bonds in shekels. This activity is routinely managed and monitored at least once a week, in accordance with the restrictions approved and validated by the Risk Management Division.

Risk management framework and methodology

As stated, tradable market risks are routinely monitored, with the frequency being determined in accordance with the nature of the activity being conducted. An estimate of the risks is made using a known and recognized methodology. The main points are as follows:

1. Interest exposures are measured and managed in terms of a change in the market value of the instruments as a result of corresponding changes in the interest curves in which exposures are taken.

2. The exposures at the option desk are measured and managed on the basis of generally accepted sensitivity ("Greeks") indices.

3. Stress scenarios:

3.1 Analysis of the sensitivity of the portfolio to the various risk factors (each risk factor separately) and an examination of the change in the value of the portfolio as a consequence.

3.2 Stress scenario – macroeconomic scenarios based on history (for example, a global scenario, based on the 2008 crisis), as well as scenarios developed in collaboration between the Risk Management Division and the Economics Department.

The table below shows the open transactions as at 31 December 2013 compared to the previous year (amounts in NIS millions):

	31 December 2013	31 December 2012
Full hedging transactions	**4,007**	4,184
ALM and other transactions:		
Interest contracts	**349,335**	308,208
Currency contracts	**230,364**	203,033
Contracts in respect of shares, share indices and commodities	**86,925**	52,389
Total	**670,631**	566,814

For details regarding the accounting policy for recording the balances, income and expenses of these types of instrument, see Note 1m –Significant Accounting Policies in the financial statements.

4. Aggregate exposure to market risk – interest, basis, shares as reflected in the Value at Risk model

The VaR limits are determined, both on the economic value of the Group including overseas subsidiaries and the effects of the exposure in VaR terms, and on the components remeasured at market value (MtM) which affect the profit and loss of the Bank (including the Bank's commercial portfolios).

Below is the estimated VaR at Group level in NIS millions:

	VaR of economic value		VaR of mark-to-market portfolios	
	31 December 2013	31 December 2012	**31 December 2013**	31 December 2012
Actual	**126**	142	**53**	41
Limit	**500**	500	**400**	400

In 2013, VaR on the economic value ranged from a maximum of NIS 157 million and a minimum of NIS 92 million, and the VAR on the portfolios remeasured at market value ranged from NIS 71 million to NIS 30 million, respectively.

In 2013, the Group complied with the VaR restriction prescribed by the Board of Directors.

Marketable credit nostro risks

Leumi is exposed to credit and market risks of countries, banks and financial institutions in Israel and abroad. In addition, the Bank invests to a limited extent in asset-backed instruments (CLO, MBS and ABS).

The Group exposure policy for foreign financial institutions is a part of the policy for managing market risks and marketable credit risks. This policy defines guidelines, risk limits on credit/counterparty exposures and authorities. The policy prescribes that most exposures will be to large banks that are systemically important to their country and to banks with a relatively high credit quality with an emphasis on dispersal of the portfolio.

Risk management in the exposure to financial institutions and to countries is effected through two credit committees headed by the Capital Market Division and in collaboration with the Risk Management Division.

- Limits Committee for activity *vis-à-vis* countries – this determines exposure limits for countries on the basis of economic analysis.

- Marketable Credit Risk Committee – this determines the exposure limits for financial institutions in accordance with the prescribed policy and market conditions.

The quality of the portfolio is monitored by the Risk Management Division and risk analyses and scenarios for the examination of risk focal points which are discussed in the Upper Market Risk Committee and in the Risk Management Committee of the Board of Directors.

Exposures to liquidity risk

Liquidity risk

Liquidity risk is the risk created due to the uncertainty relating to the possibility of raising funds and/or unexpectedly realizing assets within a short period, without incurring any material loss.

Liquidity risk management policy

In accordance with Bank of Israel directives, the Bank implements an overall policy for managing liquidity risk, the purpose of which is to support the achievement of business goals, while evaluating and limiting losses that may arise from exposure to liquidity risks. The liquidity risk management policy is aimed at maintaining a high level of liquidity through investment in quality assets at a high level of liquidity and via a deliberate policy of raising stable and varied funds, with an emphasis on raising deposits from a large number of customers for various terms, including long terms.

Liquidity management policy at Group level is based on the 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 the obligatory directives of the relevant regulatory authorities.
- The subsidiaries may rely on, amongst other sources, the use of credit lines from Leumi, subject to prior arrangement, and subject to regulatory limits.

In accordance with the abovementioned, the principles of the Bank's policy in the area of liquidity management were adopted by the overseas subsidiaries, subject to the local regulatory provisions in each subsidiary. In each of the Bank's overseas subsidiaries, the liquidity management policy is approved by the board of directors of the subsidiary. In the context of this policy, restrictions are prescribed, and compliance with the restrictions is examined with the Market and Liquidity Risk Management Committee both in the subsidiaries, and in Israel.

As part of the day-to-day management, liquidity risk is measured using an internal model whose purpose is to examine and monitor the liquid resources at the Bank's disposal under various scenarios, including stress scenarios. In addition to the model outlined above, the Bank operates an additional system of indices for early warning of unusual and unexpected developments in the liquidity position.

As part of assessments for the crisis positions, a system of qualitative and quantitative indicators has been defined, indicating an unusual development or deterioration in the liquidity position and an updated contingency plan has been drawn up including 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.

Sources of financing

The composition of the Bank's assets and liabilities continues to point to high liquidity, as a result of a policy of raising stable and varied sources and a policy of investing surplus liquid means in quality assets.

Surplus liquid means in Israeli currency are invested primarily in deposits in the Bank of Israel amounting to some NIS 27.1 billion and in securities, some NIS 37.7 billion, principally in government debentures. Surplus liquid means in foreign currency are invested primarily in debentures amounting to some NIS 22.1 billion, and in bank deposits, some NIS 11.6 billion.

The balance of public deposits in the Bank, not including subordinated notes, fell during 2013 by NIS 2.0 billion, (0.7%), and after canceling the effect of exchange rate differentials, the increase was NIS 4.7 billion, 1.6%. Most of the increase was in the unlinked shekel segment amounting to NIS 5.0 billion, 2.8%, while, in the foreign currency and foreign currency linked segment, there was a decrease of NIS 7.0 billion, (6.4%), and after canceling the effect of exchange rate differentials, the decrease was NIS 0.3 billion, (0.3%).

Monitoring liquidity risk

Pursuant to a Proper Conduct of Banking Business Management Regulation of July 2013, the Bank began to measure and manage liquidity risk via the liquidity coverage ratio (LCR), under a range of scenarios which examine the Bank's liquidity position in the ordinary course of business and under stress scenarios. The aim of the scenarios is to examine and monitor the liquid resources at the Bank's disposal in foreign currency and Israeli currency sufficient to address all liquidity requirements in a stress scenario of liquidity lasting one month. The rate of change in the balance of deposits and credit for the whole payment period, under different scenarios, is determined in accordance with various parameters, depending on the level of severity of the scenario, on the basis of the Basel III directives and the discretion of judgment of business factors. It should be pointed out that the stress scenarios are more severe than anything the Bank has experienced in the past and the assumptions of these scenarios are not based on any historical data. Measurement is made for the shekel and foreign currency sector separately and the Bank is required to comply with a liquidity ratio higher than 1 (a liquidity gap of more than 0). In addition, the Bank employs forecasts with regard to the current flow of cash, monitoring trends in various segments of deposits, monitoring concentrations of depositors, monitoring the Bank's mobilization costs and the system of warning lights which can indicate a change in the Bank's liquidity position.

In addition, the Bank has begun to monitor the net stable funding ratio (NSFR). This index is the ratio of the Bank's total stable financing sources to the total uses that the Bank is expected to continue to finance, assuming a stress scenario with a time horizon of one year. The Bank of Israel does not currently require compliance with a ratio of more than 1 as required by the Basel III directive.

Fair value

In accordance with the directives of the Bank of Israel, the fair value of all financial instruments, i.e. all the monetary assets and liabilities of the Bank and of its subsidiaries, is shown in Note 18C to the Financial Statements. The fair value of a financial instrument is defined as the price paid by a buyer to a seller in an arm’s length transaction.

When there is an active market, the market price constitutes the fair value. The price of certain securities is determined on the basis of assessments obtained from a third party, while, for derivatives, the value is determined on the basis of models. Market prices do not exist for a significant portion of the financial instruments of the Bank and its subsidiaries. In the absence of a market price, the fair value is an estimate, based on the present value of cash flows, as specified in Note 18C.

Fair-value estimates are based on the conditions existing on the date of the Financial Statements and do not necessarily represent future fair values.

The Board of Directors of the Bank has prescribed a limit of US$ 600 million for the total of transactions whose fair value is determined by the Bank on the basis of quotations received from the counterparty to the transaction. As a rule, these are financial institutions of high repute in the capital markets, who meet the criteria prescribed by the Bank Management.

The calculation of fair value is also based on a subjective assessment. Therefore, great care must be exercised when using this information, since it cannot indicate the economic value of the Bank and its subsidiaries, nor can it be used for comparisons between different banks.

It should be noted that data relating to fair value do not take into account the effect of taxes in the event of a positive or negative gap between the fair value and the book value of assets and/or liabilities shown on an accrual basis.

The data appearing in Note 18C to the financial statements show that the fair value of financial assets at the end of 2013 was NIS 1,591 million higher than the balance sheet value (in 2012, higher by NIS 1,234 million), while the fair value of financial liabilities was NIS 4,406 million higher than the balance-sheet value (in 2012, higher by NIS 4,645 million). The majority of the gap derives from the fact that the decrease in interest on liabilities was greater than the decrease in interest on loans, due to an increase in the risk margin.

The change in the fair value of monetary assets and liabilities beyond that recorded in the financial statements in 2013 derives mainly from the decrease in interest rates in the economy, and particularly, in the unlinked shekel segment, similar to the decrease in 2012.

Operational risks

Leumi Group operates in a wide range of financial activities, and, accordingly, is exposed to operational risk, including, *inter alia*, risk of embezzlement and fraud, legal risks, compliance risk, data technology risk, business continuity and data protection.

An operational risk is defined as the risk of a loss resulting from inadequate or failed internal processes, people, systems, or external events. This definition includes legal risk, but not strategic risk and image risk.

A significant pillar in the range of operational risks is data technology risks, which are liable to expose the banking corporation to impairment in business activity due to system failure, and, as a consequence, to impairment of goodwill.

Operational risks in Leumi Group are managed with systemic vision, using a consistent and systematic group methodology which delineates the Operational Risk Management Branch in the Risk Management Division, adapting to the nature, size and complexity of each organizational unit in the Group. Operational risk management relies on a proactive process of identifying, evaluating, measuring, monitoring, reporting and controlling/reducing material risks, which is carried out in all divisions of the Bank.

Operational risk management in Leumi Group relies on three lines of defense, similar to the other risks. Responsibility for operational risk management falls upon the managements of the divisions and subsidiaries (first line of defense) and includes: selecting from the alternatives of accepting the risk, a change in controls, a change in the scope of activity or a transfer of risk. The Operational Risk Management Department and the Compliance and the Prohibition of Money Laundering and SOX Department in the Accounting Division and the Legal Counsel Division in relation to legal risks, represent a second line of defense. The third line of defense is the Audit Division. The latter two lines of defense have an independent hierarchical reporting structure in the lines of business in which risk exists.

Operational risk management policy is on a group basis and is intended to minimize losses, taking into account risk tolerance and maintain long-term operating stability. Operational risk management is an integral part of the organizational culture and business and operational activity in the Group.

Risk appetite/tolerance in the Bank is defined for operational risks. In risk tolerance, loss restrictions, the Bank determines limits on loss are determined that the Group will be prepared to absorb in various scenarios, and in a number of significant products/activities.

Corporate governance

Monitoring and supervision of operational risk management in the Group is carried out through the Board of Directors, the operational risk management function in the Risk Management Division, and the Operational Risk Committees and Controller Department (coordinators of the subject in the first line of defense units) and officers in charge in the divisions are responsible for the formulation of risk management in the processes under their responsibility. In addition, there are various forums which convene on the subject of operational risk under the leadership of the Operational Risks Manager, in which representatives of the business entities and subsidiaries (control officers), the Legal Counsel Division and the Compliance and Enforcement Department participate. These forums represent a platform for sharing knowledge, the drawing of lessons from failure events inside and outside the organization and discussion on strategies for reducing risk.

In addition, various forums convene to discuss operational risk management, led by the Operational Risk Manager, attended by representatives of all the business entities and subsidiaries (the risk controllers), the Legal Division and the Compliance and Enforcement Department. These forums constitute a platform for sharing knowledge, drawing conclusions from failure incidents inside and outside the organization and discussing strategies for reducing risk.

The independent function of operational risk management

The Operational Risk Management Branch in the Risk Management Division is responsible for the Group's policy outline – which is discussed and approved by the Board of Directors –planning and development of methodology and tools, methods and a working framework for operational risk management, real-time partnership in examining risks in projects and in material new products, assimilation of an operational risk management culture, reporting to the Board of Directors and senior management, and support and professional guidance of the representatives of the first line of defense.

Methodologies, processes, methods and tools for operational risk management

The methods and tools for operational risk management in Leumi are examined and updated from time to time, leveraging professional knowledge from Israel and around the world, and as a result of regulatory directives of the Bank of Israel and other supervisory bodies. Presented below is a description of the range of measures taken by the Bank in order to strengthen the operational risk management.

The Group has defined an operational risk management policy document which forms a basis and working framework for risk management, and, in the spirit of the document, procedures and methods have been determined. An updated policy document was approved in December 2013. In addition, methodological tools have been assimilated for the management and control of operational risks. Within the Group, procedures supporting the reporting of loss and near-loss events and the examination of the effectiveness of controls have been prepared.

In addition, a methodology for risk management in material new projects and products has been developed, defining a structured process of mapping and risk management in the project and its products.

Over the second quarter of 2012, a three-year round of a risk assessment survey on central work processes was conducted, in the course of which, prioritized reduction programs were determined. The survey was conducted in two channels – the assessment of risk and the construction of prioritized reduction programs in business processes and supporting processes. A special emphasis was placed on IT procedures.

An ordered risk assessment, on the basis of the survey, enables the Bank to understand its own risk profile, to designate resources and strategies for managing risks more effectively, and to assess the amount of capital required in respect of operational risks. The risk assessment is a self-evaluation by content experts who are acquainted with the business activity in which the risk is inherent, and combines a qualitative and quantitative assessment. The quantitative assessment relates to potential monetary damage, and the qualitative assessment covers all direct and indirect damage that could occur when the risk materializes, with reference to structured risk, to the existing controls, and as a result, to the residual risk.

The Bank is taking steps to establish a robust culture of operational risk management among all employees and managers in the Group. Within this framework, assimilation and training procedures are carried out in designated training sessions for managers and employees, integrating the project in a variety of banking courses and the construction of a designated operational risk management portal.

A further means of risk management is the analysis of stress scenarios, which are assessed and monitored, and for which evaluation and reduction programs are established. Bank Leumi is continuing to strengthen its ability to continue business activity in the event of the materialization of broad operational scenarios, such as war and earthquake. The Bank, however, has computers which are protected against missiles and earthquake, an emergency program for the continuation of the Bank's activity in the event of scenarios of this type.

The allocation of capital in respect of operational risks is intended to act as an absorption cushion for unexpected risks. The regulatory capital is calculated using the standardized approach.

At the same time, an assessment is made of the economic capital on the basis of a self-evaluation of operational risks, with the results of the calculation constituting a basis for challenging the regulatory capital. The assessment of the economic capital is made using an internal model of the loss distribution approach (LDA).

Operational risk is managed using a designated system, supporting the documentation of risks, controls and reduction programs. In addition, the system enables the gathering and analysis of internal loss and near-loss events. The stored data supports the decision-making process with regard to the material risks and the prioritization of the reduction operations.

Data technology risk

Data technology is a central component in the proper operation and management of a banking corporation, inasmuch as the data, in all its aspects and implications, has a decisive effect on the Bank's stability and development. Data technology risks apply to the operation of data systems in production, broad data technology processes and new activities (projects and systems).

A policy document has been prepared on information technology risk management, which defines the principles for technological risk management and includes the organizational framework, areas of operation and responsibility of the various functions in the Group and the work processes necessary for managing technological risks.

An assessment of the level of operating risk in the system's ongoing operation is integrated into the risk management process. An analysis of the results of risk assessments facilitates identification of high-risk systems. In accordance with the risk assessment, a multi-year work program is designed to carry out safety surveys and controlled penetration attempts, and a reduction program is determined accordingly.

In addition, a methodology for assessing risks in data systems development projects has been implemented and assimilated, the findings are analyzed, and recommendations for reducing the level of exposure is determined.

Data protection risk

Data protection risk management in Leumi is executed on the basis of Leumi's data protection policy.

Pursuant to Proper Conduct of Banking Business Management Regulation no. 357, Leumi conducts a data protection survey in critical systems of the Bank. As part of the survey, safety reviews and system penetration tests are carried out for detecting exposures and reduction plans are established accordingly.

The management of data protection risks supports the solution to threats and risks and maintaining Leumi's data assets and data technology systems.

Data protection contends with challenges emanating from threats inherent in developing technologies.

Data protection is made ready, among other things, *vis-à-vis* the increase in threats and attacks, including cyber-attacks, using an international model for mapping and risk management, the implementation of controls and hedging of risks.

For further explanation on the subject of cyber-risks, see below.

Business continuity risks

Bank of Israel directives require banks to take action to ensure business continuity in an emergency. The Bank's computer system relies on two computer centers. The main center is located in Kiryat Hamachshavim in Lod – underground and protected against missiles, earthquakes and biological and chemical attack – and a secondary underground center in Tel Aviv. In addition, Leumi has set up an underground emergency location for the Bank's trading room in the Hamachshavim Compound in Lod.

There is another site in Jerusalem which as a third backup for data.

The Bank prepares itself for disaster recovery and continuity of its business activity. Activity is comprised of three layers:

- Technological infrastructure;
- Action plans and procedures;
- Periodic emergency drills.

The main activities in the area of business continuity carried out were as follows:

1. A disaster recovery survey was conducted – a project whose aims are: the charting of the present preparedness for computer failure, finding alternatives for improving/upgrading the disaster recovery plan/business continuity plan, specifying definition of gaps between the existing preparedness and alternatives. This activity will also continue in 2014.
2. Leumi practice drill as part of the "Oref Eitan 1" national emergency drill, Leumi carried out an emergency exercise in the event of an escalation scenario or missile attack. The exercise was carried out successfully, maintaining complete availability and continuity in the provision of service. As part of the exercise, the following activities were carried out: A practice drill of the emergency site of the capital market, the establishment and operation of a mobile branch in the Keshev installation and a national exercise of retreating to shelters.
3. Prioritization of critic processes at the Bank level.
4. Updating policy documents and procedures (business continuity policy, crisis management team procedure, crisis operation team procedure, disaster manager procedure, etc.)
5. Adaptation to the Bank of Israel's Banking Conduct of Business Management regulations for business continuity - end of a triennial round.
6. Completion and improvement of an emergency mobile bank branch.
7. Analysis of the business effects in the Division in accordance with the work program - end of a triennial round.
8. Technological and unit exercise drills were carried out in accordance with annual exercise programs.

Data security and cyber-attack risks – Leumi's business activity relies largely on its data systems, the availability of the systems, the reliability of the data and the maintenance of the confidentiality of the information essential for orderly business activity. With the advance of technology, the level of risk to Leumi and its customers increases. In aspiring to progress and excellence, new technologies are integrated into the banking core, as well as in the end-user systems in Leumi and among its customers. These technologies create uncertainty and raise the level of risk from cyber-attacks.

Bank Leumi, as a leading financial organization, is an attractive target for various attackers. The computer systems, communication networks and our customers' devices have come under attack and will continue to be vulnerable to cyber-attack, viruses, malware, phishing, and other exposures intended to cause damage to service, or steal or corrupt data.

Leumi regards the Bank's data as an important asset and invests much effort in applying supervision and control mechanisms and procedures.

Reporting as forward-looking information – In recent years, it has been possible to distinguish an increase in the scale of cyber threats worldwide. Attacks have taken place against national infrastructures, government bodies and corporations, both in Israel and around the world.

The attacks have been carried out by various players, from employees in the organizations, through organized crime, to attacks instigated by nations and individuals for political motives.

As a part of preparations for dealing with cyber-threats, a survey was carried out in order to review Leumi's resistance. As a result of the survey, Leumi began a multi-year process to improve its defensive capability against cyber-threats.

In addition, two potential scenarios on the subject of a cyber-attack have been constructed – disruption of data and leakage of data, and risk tolerance indices for these two subjects have been defined.

It is important to note that Leumi's operating preparedness in the face of cyber-attacks is a good level, and consequently, till now, cyber-attacks have not caused any significant damage to business activity.

In our opinion, the escalation of cyber-threats will continue in coming years, despite the fact that there has been a restructuring at the sectoral, national and global level in an attempt to create defensive, technological, regulatory and cooperative frameworks.

Compliance, Prohibition of Money-Laundering and Prohibition of the Financing of Terrorism

In 2001, at the request of the authorities, the Compliance Department commenced operations in the Group, pursuant to the requirements of the authorities, and a chief compliance officer was appointed to be responsible for complying with the obligations pursuant to the statutory provisions relating to the prohibition of money laundering and the prohibition of the financing of terrorism.

The complexity and development of banking activities require the Bank to comply strictly with all obligations applicable to a banking corporation in its relations with its customers, by virtue of primary legislation, regulations, orders, permits and Bank of Israel directives.

Proper Conduct of Banking Business Directive No. 308 obligates banks to enforce consumer directives, i.e. the laws, regulations, and directives governing banking activities regarding the Bank's relations with its customers, including the prohibition of money laundering and the prohibition of financing of terrorism.

In accordance with this Directive, a review of infrastructure is carried out every five years, in which consumer directives and the risks of the occurrence of events deviating from the directives are mapped out, and controls are defined to prevent their occurrence.

A decentralized compliance model and automated tools and systems required for the compliance functions have been implemented in Leumi.

For the effective management of the subject, a compliance community has been set up in Leumi, comprising divisional compliance managers, regional compliance managers in the lines of business and compliance trustees for focused treatment and control of the areas of compliance, the prohibition on money-laundering, the prohibition on the financing of terrorism, administrative enforcement and American customers.

The Compliance and Enforcement Department is in regular contact with the Bank's subsidiaries in Israel and overseas, for the purpose of monitoring the implementation of compliance, including the prohibition of money laundering, the prohibition of financing terrorism in U.S. customers and the "declared money" policy. The department operates in accordance with the Group compliance policy document, which is periodically updated in accordance with local and international trends. The last version of the policy document was approved by the Board of Directors in January 2013.

In 2013, the Bank continued activities required for the implementation of the statutory provisions pertaining to the prohibition of money laundering and the prohibition of the financing of terrorism, including: steps for improving data, the dissemination of publications and lessons learnt to the various units, developing and improving computer systems, and participation in training activities, to heighten awareness of this subject and the assimilation thereof among employees of the Bank.

On 17 February 2013, the Supervisor of Banks published a final version of the file of questions and answers for implementing the Prohibition of Money Laundering Order and the Proper Conduct of Banking Business Management Regulation no. 411. The file represents a summary of the binding positions and interpretations of the Supervisor of Banks with regard to the implementation of these legislative provisions. As a result of the publication, the department is taking steps to make the required adjustments in accordance with this document.

On 29 October 2013, the Knesset Constitution, Law and Justice Committee approved the version of the amendment to the Prohibition of Money Laundering Order (Duties of Identification, Reporting and Record Management of Banking Corporations for the Prevention of Money Laundering and the Financing of Terrorism), 2001 (hereinafter, the Order). Following approval, the department began an exercise of charting the amendments to the Order and forwarding them to the development factors for executing the requirements and adapting the automated systems, as well as adapting the working procedures. The Order was published in *Reshumot* on 2 February 2014 and will become effective in August 2014.

Enforcement

In January 2011, the Efficiency of Enforcement Procedures in the Securities Authority Law (Legislative Amendments), 2011, was passed in the Knesset. The object of the law, which is detailed in the explanatory notes, is the improvement of efficiency of enforcement over the legislative provisions in the area of securities laws. In the context of this legislation, it will be possible to impose various sanctions on a corporation, including its violating officers and employees, that breaches the relevant provisions.

Further to the law, the Securities Authority published a document of criteria for recognition of an internal enforcement program in the field of securities and investment management (hereinafter: "document of criteria").

In the document of criteria, the Securities Authority instructs the corporation to appoint an officer to be in charge of enforcement. His function, according to the document of criteria, is to be responsible for the implementation of the enforcement program.

The Chief Compliance Officer of the Group was also appointed by the President and Chief Executive Officer to serve as head of Compliance and Enforcement and has the authority and means to implement the legislative provisions relevant to this area.

On 20 January 2013, the Board of Directors was presented with the draft internal enforcement program, which was built according to guidelines determined in the document of criteria. In 2013, the implementation of the enforcement program began, including, *inter alia*, continuing to conduct surveys of compliance with the relevant legislative provisions including mapping of the gaps in this area, and formulating reporting, assimilation and control mechanisms.

Foreign Account Tax Compliance Act– FATCA

In March 2010, the Internal Revenue Code in the United States (the U.S. Income Tax Law) was amended, so as to bring into effect a reporting regime, which aims to compel foreign financial institutions (FFI) to transfer information regarding accounts held by U.S. customers.

As a part of the Bank's preparedness for implementing the law in Leumi Group, the division is acting in conjunction with the Finance and Economics Division Legal Consulting Division in circulating procedures and circulars and in assimilating policy regarding the arrangement of the subject of identifying, detecting and dealing with U.S. customers.

As of date, the FATCA regime will come into effect on 1 July 2014.

Legal risks

The Bank of Israel defines legal risk as the risk of loss resulting from the inability to legally enforce the performance of an agreement. The legal risks are part of the operational risks.

Legal risks derive from four main areas:

- Legislation risks - Risks attributable to the Bank's activity, if it does not comply with a primary or secondary legislative directive, a regulation of the Bank of Israel or a directive of other qualified authorities.
- Contractual communication risks - Risks attributable to the Bank's activity with customers, suppliers and other factors with whom the Bank contracts in various agreements, if it is not backed by an agreement fully regulating the Bank's rights, or that the agreement is not fully enforceable.
- Court ruling risks – Risks deriving from the Bank's activity if it does not comply with a precedential court ruling.
- Risks attributable to legal proceedings conducted against the Bank.

The Group also implements a program for managing legal risks, which aims to detect, prevent, manage and minimize the legal risks. The program includes policy documents and an interface between the Legal Division and units of the Bank, as well as internal procedures applicable to the Legal Division, the purpose of which is to ensure that legal counseling provided in the Bank is professional and up-to-date. The policy document was updated at the end of 2012.

With regard to the Bank’s subsidiaries in Israel and abroad, a general policy has been determined to manage risks in the framework of designated policy documents. Each subsidiary has prepared an internal procedure for managing legal risks that correspond with its activity and the Group policy on the subject. The internal procedures prepared by the subsidiaries as aforesaid, have been approved by the Legal Division and in the boards of the subsidiaries. According to the policy documents, the subsidiaries are required to refer certain subjects for appropriate legal advice. In addition, the companies send six-monthly reports to the Legal Risk Officer at the end of the second and fourth quarters each year, as well as immediate reports, as required in the policy documents. The reports were sent in a consistent format prepared in the Legal Division and updated in 2012. In 2013, the document policy for legal risk management in the overseas units was updated and its assimilation will continue in 2014.

The legal risk management program places emphasis on:

- Preventing and minimizing legal risks;
- Identifying sources of material legal risks and how to deal with them;
- Preparing appropriate agreements, guidelines and procedures;
- Examining statutory provisions (including case law) and regulatory directives, and their implications on the work of the Bank.
- Drawing conclusions on various matters and implementing of these conclusions drawn in legal documents used in the Bank, as well as disseminating opinions on these subjects to the relevant units in the Bank.

In order to conduct the legal risk management program, various officials and committees operate in the Legal Counsel Division, headed by the Chief Legal Counsel who is the Legal Risk Officer, whose function is to locate and examine new legislation and legal rulings that have repercussions for the work of the Bank and coordinate the way in which they will be dealt with. New regulatory directives (primary legislation, secondary legislation, and directives from authorities) are identified and, if necessary, dealt with, even at the stage of being a proposed law.

The activity of each of the abovementioned officials and committees is organized in an internal work procedure of the Legal Division. The procedures stipulate, *inter alia*, the information flow among each of the abovementioned officials and the management of the division and the legal risk team which operates in the division.

Linkage Status, Repayment Periods and Liquidity Status

A. Linkage Status

In accordance with the policy for the management of assets and liabilities on a linkage basis, the available capital – which is defined as the total of capital sources and certain reserves, less investment in consolidated companies and fixed assets – is invested in unlinked shekel assets, CPI-linked assets and foreign currency and foreign currency-linked assets. The financing of all of the Bank's overseas investments from foreign currency sources, back-to-back, prevents basis exposure in respect thereof.

A summary of the linkage balance sheet position, as it appears in note 16 to the financial statements, is as follows:

The linkage balance sheet is as follows:

	As of 31 December 2013			As of 31 December 2012		
	Unlinked	CPI-linked	Foreign currency(2)	Unlinked	CPI-linked	Foreign currency(2)
	NIS millions					
Total assets (1)	**227,187**	**57,812**	**112,180**	216,766	60,341	120,050
Total liabilities (1)	**205,407**	**58,571**	**114,950**	197,183	62,127	120,874
Total exposure in the segment	**21,780**	**(759)**	**(3) (2,770)**	19,583	(1,786)	(3) (824)

(1) Includes future transactions and options.
(2) Includes foreign currency linked.
(3) The excess of liabilities in foreign currency derives mainly from a hedging transaction against the tax exposure in respect of investments in overseas units of the Bank, investment in shares and reserves classified as a noninterest-monetary item, and also in respect of hedging future income in foreign currency.

Day-to-day management and reporting of the exposure of the Bank to basis risks is conducted according to the economic approach including adjustments and additions to the accounting approach shown above. The basis exposure, calculated according to the economic approach, is detailed in the chapter, "Exposure to Risks and Methods of Risk Management".

In 2013, there was a decrease of some NIS 5.6 billion in total deposits from the public (including subordinated notes and capital notes). In total credit to the public, there was no material change. Investments in securities and debentures increased by some NIS 5.8 billion, and credit to banks decreased by some NIS 10.4 billion.

The main changes that occurred in 2013 in the principal activity divided into linkage segments were as follows:

The unlinked shekel segment

The percentage of the financial assets in the unlinked shekel segment to total financial assets is some 57%.

Most of the activity in the segment is for short periods, up to one year.

Total credit to the public increased by some NIS 8.8 billion, some (6.4%).
Total deposits in banks, net, decreased by NIS 9.5 billion, and the total investment in securities increased by some NIS 7.1 billion.

In 2013, total shekel deposits increased by NIS 1.1 billion, 0.7%. This increase includes the repayment of capital notes and subordinated notes amounting to NIS 1.7 billion.

Total net balance of derivative transactions in the segment as at 31 December 2013, was some NIS 23.7 billion, an increase of NIS 4.1 billion compared to December 2012.

The CPI-linked segment

Total credit to the public fell by some NIS 1.3 billion, some 2.4%. Total investment in securities fell by NIS 1.4 billion.

There was no material change in index-linked deposits, including subordinated notes.

The net balance of derivative transactions in the segment as at 31 December 2013, amounted to some NIS 2.4 billion, a decrease of NIS 3.8 billion compared to December 2012.

Foreign currency and foreign currency linked segment

The percentage of financial assets in the foreign currency segment as a percentage of total financial assets is 28%.

Credit to the public, which constitutes only some 40% of the total deposits of the public in the segment, decreased by NIS 8.2 billion, a reduction of 17% and after canceling the effect of exchange rate changes, a reduction of 11%.

Investments in securities in foreign currency amounted to NIS 22 billion, with no material change compared with December 2012.

Deposits in banks, net, fell by some NIS 0.9 billion.

From the beginning of 2013, there was a decrease of some NIS 7 billion, 6.4% in total deposits of the public in foreign currency, which derives mainly from the effect of changes in exchange rates.

According to past experience, a large part of deposits in the foreign currency segment, deposited for periods shorter than one year, including deposits on demand, are re-deposited in the Bank in a continuous and constant process.

Activity in future transactions has a material impact on liquidity in the foreign currency segment. Total net future transactions in foreign currency against shekels amounted to some NIS 25.8 billion as of 31 December 2013, an increase of some NIS 0.6 billion, compared with December 2012.

B. Repayment periods

During 2013, as in recent years, the Bank was characterized by a high level of liquidity in shekels. This was partially as the result of a policy directed by the Bank to raise stable and varied sources of funds, by means of public and private offers and raising deposits from a large number of customers for various periods including long-term.

Some 27% of the Bank's total assets are deposited for short periods in banks and invested in marketable securities, mainly in government debentures.

Total liquid assets in 2013 were significantly higher than total short-term liabilities and the Bank complied with all liquidity limits for the various scenarios. This was in accordance with the policy whose aim is to ensure stability also in extreme theoretical stress scenarios.

The following table shows a future cash flow of the assets and liabilities according to repayment periods and according to basis of linkage (including derivative instruments and not including non-monetary items) (For further information, see Note 17 to the Financial Statements).

Pursuant to a circular of the Bank of Israel, cash flows in respect of liabilities with a number of repayment dates will be classified according to management's assessment at its discretion or the earliest forecast repayment date.

According to a Bank of Israel circular from September 2013, a banking corporation is required to present the cash flows in respect of assets and liabilities distinguishing between Israeli currency (including Israeli currency linked to foreign currency) and foreign currency. In addition, cash flows in respect of cleared derivative instruments, net, will be classified to Israeli currency or to foreign currency according to the currency in which the clearing was made. Off-balance sheet amounts of these derivative instruments should not be reported. Comparative data for 2012 have been reclassified accordingly.

	As at 31 December 2013		
Surplus of assets over liabilities*	Israeli currency	Foreign currency	Total
Period remaining to maturity:	NIS millions		
Up to 1 month	**(77,787)**	**(36,205)**	**(113,992)**
From 1 month to 1 year	**22,649**	**6,695**	**29,344**
From 1- 5 years	**39,438**	**22,358**	**61,796**
From 5 - 10 years	**27,232**	**5,634**	**32,866**
More than 10 years	**39,988**	**2,403**	**42,391**
Without maturity date	**724**	**(44)**	**680**
Total	**52,244**	**841**	**53,085**

	As at 31 December 2012		
Surplus of assets over liabilities*	Israeli currency	Foreign currency	Total
Period remaining to maturity:	NIS millions		
Up to 1 month	(52,322)	(36,079)	(88,401)
From 1 month to 1 year	2,406	7,482	9,888
From 1- 5 years	36,469	23,273	59,742
From 5 - 10 years	22,073	5,422	27,495
More than 10 years	34,449	2,673	37,122
Without maturity date	(384)	283	(101)
Total	42,691	3,054	45,745

* After offsetting surplus (deficit) balances in respect of derivatives.

A description of the key points of the policy, the means of monitoring and implementing the policy, and the limits used in the management of market risks, including basis and liquidity risks, are presented in the chapter, "Exposure to Risks and Methods of Risk Management" above.

In the Israeli currency sector, there was an increase in the excess of liabilities over assets for a period of up to a year, mainly as a result of an increase in the balance of short-term deposits. At the same time, there was an increase in the excess of assets over liabilities for a period above one year, arising from an increase in balances of credit to the public and a reduction in the deposits of the public in this period. There were no material changes in the foreign currency sector.

C. Liquidity Position and Funding

Liquidity position and raising funds by the Bank

The surplus liquidity of the Israel banking system continued to be high in 2013. In order to absorb the surpluses, each day, week and month, the Bank of Israel holds monetary tenders. This in complementary manner to the short-term loan tenders.

After a prolonged suspension, in April, the Bank of Israel announced that, in 2013, it would purchase some US$ 2.1 billion in order to offset the effect of gas royalties on the exchange rate. The foreign currency purchases have an extensive impact on liquid shekel surpluses.

The composition 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, including for the long term.

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.

The total balances of the banking system (current accounts and monetary deposits) in the Bank of Israel at the end of December 2013 stood at NIS 127 billion, similar to the end of 2012.

The total balances of Leumi (current accounts and monetary deposits) in the Bank of Israel at the end of December 2013 stood at NIS 27 billion, compared with NIS 36 billion at the end of 2012.

At 31 December 2013, the net balance of cash and deposits with banks amounted to some NIS 32.9 billion, compared with NIS 42.4 billion at the end of 2012, a decrease of some 22%.

In addition, the Bank has a securities portfolio of some NIS 57 billion, invested mainly in Israeli government debentures, foreign government debentures, and debentures of banks overseas. This is in comparison to the balance as at 31 December 2012 amounting to NIS 49 billion.

During the period under review, the total off-balance sheet monetary assets of the customers increased by NIS 78 billion to NIS 574 billion.

Legal Proceedings

1. Civil Proceedings

1.1 The Bank is a party to legal proceedings, including petitions for leave to approve class actions, brought against it by customers and former customers of the Bank, and various third parties considering themselves prejudiced or harmed by the Bank's activity during the ordinary course of its business.

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

The grounds for claims against the Bank are different and varied, including assertions as to the non-execution of instructions or their late execution, petitions for approval of attachments imposed by third parties on assets of debtors that according to them, are held by the Bank, assertions that interest charged is not in accordance with the interest rates agreed upon between the Bank and the customer, interest rates deviating from those permitted by law, errors in the dates of debiting and crediting accounts in respect of checks drawn on them, assertions in connection with the charging of commissions, assertions relating to securities, labor relations, drawing checks without cover, and failure to honor checks.

For claims in an amount exceeding 1% of the shareholders' equity of the Bank on 31 December 2013, of about NIS 270 million, see also additional details in note 18 to the financial statements.

1.2 As part of measures taken to recover debts during the ordinary course of its business, the Bank initiated, *inter alia*, various legal proceedings against debtors and guarantors, as well as proceedings to realize collateral. The Financial Statements contain allowances for credit losses that were made by the Bank on the basis of an assessment of all the risks involved in the credit to the various sectors of the economy and taking into account the extent of the information concerning the relevant debtor/guarantor with regard to his financial strength and the collateral given to the Bank to secure repayment of the debt.

1.3 On 29 January 2013, the Tel Aviv District Court approved a request for the repudiation of a claim without an order for costs and instructed the rejection of the petition for approval as a class action, which had been submitted on 7 March 2012, against Automatic Bank Services Ltd. (hereinafter: "ABS") and the banks, its shareholders, and against Casponet Ltd and its shareholders, the amount of which was estimated by the petitioners at NIS 2.2 billion. The plaintiffs' claim was that the defendants collect excessive withdrawal commissions through limiting the withdrawal amounts in ATMs located at a distance from a bank branch, so that a customer who requests to withdraw an amount larger than the withdrawal ceiling is forced to make a series of withdrawals, in respect of each of which it pays a high commission.

1.4 On 15 January 2014, the Tel Aviv District Court approved the request of the petitioners to repudiate, without an order for costs, a petition for approval as a class action, which had been submitted against the Bank on 6 February 2013, amounting to NIS 12 billion, alleging that the Bank had collected excessively high interest, contrary to the "*Heter Iska*" (loan agreement under Jewish law) received from the Rabbinical Court for Monetary Affairs, which caused damages to all customers who took loans from the Bank while relying on the "*Heter Iska*".

On 2 January 2014, the Supreme Court rejected the appeal submitted by the plaintiff, on the judgment which rejected its approval of the petition for approval as a class action, which had been submitted against the Bank on 8 September 2011, amounting to NIS 200 million, in a claim, according to which, until the reform in bank commissions, the Bank charged its customers a higher commission than generally agreed in its list of charges, on making a partial sale of securities during the quarter, in respect of which, a commission was charged at a fixed minimum amount per security in the list of tariffs.

2. Other Proceedings

2.1 On 26 April 2009, a ruling of the Antitrust Commissioner 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 1990's until the commencement of the Antitrust Authority's investigation into 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 submitted an appeal against this ruling. On 22 February 2011, the Commissioner's response to the appeal was submitted. On 29 July 2012, the Bank received a letter from the Antitrust Authority according to which the Antitrust Commissioner is considering publishing a supplementary ruling in relation to the transfer of information set forth in the response of the Commissioner to the appeal, but that was deleted from it at the request of the banks, according to which the transfer of information were restrictive trade arrangements. The Bank was given the opportunity to present its position to the Commissioner before the Commissioner makes a decision to issue the said supplementary ruling. As a result of negotiations conducted between the banks, agreement in principle was formulated between the parties according to which the Antitrust Tribunal would be requested to approve an agreed order which would bring to an end the proceedings arising from the investigation which led to the issuance of the ruling. According to the wording of the agreed order formulated by the parties, the ruling would be canceled, while the Bank pays the Treasury the sum of NIS 21 million (and further amounts will be paid by other banks) with the Bank having the possibility of paying the said sum (and the other banks having with respect to the amounts relating to them), instead of payment to the Treasury and subject to the conditions stipulated in the wording of the agreed order, as part of the compromise arrangements in a number of petitions for the approval for class actions pending against the Bank.

2.2 As stated in the previous financial statements, United States authorities ("U.S. authorities") are conducting wide-scale investigations into foreign banks in connection with their activity with customers who are taxpayers in the United States ("the U.S. customers"), on suspicion of a breach of United States law. As part of these investigations, which have also been conducted into the Group, the U.S. authorities have issued and are continuing to issue various subpoenas for the receipt of information and documents regarding banking services rendered by the Group to the U.S. customers.

The Bank made a provision to cover the anticipated expenses in this connection, including those of advisors, service providers and outside experts. The balance of the provision at 31 December 2013 amounts to NIS 490 million.

With regard to the total expenditure in respect of the U.S. customers, see note 25 "Other operating expenses".

This provision does not constitute an acknowledgement of any claim that might be raised against the Group by the U.S. authorities.

Ongoing contacts are being made between the Group and the U.S. authorities with the aim of reaching a solution of the matter. The Group is cooperating with the U.S. authorities, subject to the constraints of the law.

In light of the fact that there is still no certainty regarding the amount of expenditure that might be incurred by the Group on this matter, it is possible that the final expense will be significantly higher than the amount thus far included in the financial statements.

2.3 On 26 August 2013, the Antitrust Commissioner ("the Commissioner") granted the exemption regarding the joint holdings of Bank Leumi, Bank Hapoalim, Bank Discount, First International Bank and Bank Mizrahi-Tefahot (hereinafter: "the Banks") in ABS – Automatic Bank Services Ltd. (hereinafter "ABS") for a period of three years. Pursuant to the exemption, further terms were stipulated in addition to those provided in previous exemptions granted by the Commissioner. The exemption includes conditions relating to the technological interface for providing credit card transaction collection and approval services and interface services between businesses and ABS, which are developed and assimilated in ABS systems, principal of which is the provision of a possibility for rapid connection under equitable conditions and at a low cost, of various entities that are entitled under the law to connect to ABS, with effect from 1 October 2015. On 7 August 2013 and 30 January 2014, ABS signed an agreement and an amendment of an agreement to sell its automated cash-dispensing activity, subject to fulfilling the conditions precedent in the agreement, pursuant to the decision of the Commissioner on this matter. The Commissioner has yet to give his approval to the amendment of the agreement.

2.4 In March 2012, an indictment was served against Leumi Romania and against members of the credit committee of Leumi Romania, regarding a transaction in the account of a customer, who, according to the General Prosecutor in Romania, was not lawfully carried out. The indictment was submitted as a result of a complaint by the customer who alleged that he incurred damage as the result of the bank's action (the amount of the damage is not material). On 28 November 2012, the court in Romania accepted Bank Leumi Romania's arguments that the General Prosecutor in Romania had no authority to serve an indictment against it and against certain of its employees/managers, and decided to send the file back to the General Prosecutor for rewording and resubmission of the indictment. The General Prosecutor and the complainant have appealed the decision. The appeal was accepted, the case returned to the court of first instance and a date was set for discussion.

2.5 On 1 September 2013, a petition to approve the submission of a derivative claim against former senior officers in the Bank was submitted to the Economic Department of the Tel Aviv District Court. According to the petitioner, as part of the investigations of the tax authorities in the United States, representatives of the Bank and representatives of Bank Leumi USA assisted customers who are assessed for tax in the United States to enter into transactions which prevented the tax authorities in the United States from collecting taxes from their citizens. The damage incurred by the Bank, according to the petitioner, stands at hundreds of millions of shekels which the Bank intends to pay to the United States tax authorities, and at this stage, the Bank has put aside the sum of NIS 340 million, with part of the sum paid to advisors and service-providers in connection with the investigations. The petitioner claims that the former officers are responsible for the damage incurred by the Bank when they led it to take part in the illegal activity or at least, did not prevent it.

2.6 In 2010, the Securities Authority of Ontario conducted an audit in the Bank's representative office in Toronto and informed the Bank that, for the purposes of continuing the provision of security services to Canadian customers, it was obliged to arrange an exemption from the obligation to register as a trader (international dealer exemption). The Bank received this exemption in Ontario and Quebec ("the exemption").

Pursuant to the terms of the exemption, Canadian customers are not entitled to hold securities in their accounts in the bank, unless they meet the definition of "permitted clients" (*inter alia*, private customers with a financial wealth of Can$ 5 million) and even those are not entitled to hold Canadian securities in their deposits in the bank.

In a regulated process which commenced in 2011, the Bank took steps to comply with the requirements and the terms of the exemption. The Bank is currently in advanced negotiations with the authorities in Ontario and Quebec towards an arrangement whereby it will pay a monetary penalty of Can$ 1 million in respect of the apparent failure to comply with the provisions of securities and investment consulting laws, prior to the regulation of the exemption.

For details regarding claims and petitions for approval as class actions submitted against the Bank, see also note 18 to the financial statements.

Restrictions and Supervision of Activities of the Banking Corporation

1. Pursuant to legal provisions, the Bank is subject to the supervision of various authorities with regard to its various activities, and especially with regard to its overall activities, to the supervision of the Bank of Israel, specifically the Governor of the Bank of Israel and the Supervisor of Banks.

By virtue of the powers granted to the Governor of the Bank of Israel and the Supervisor of Banks, various permits and approvals are issued by them from time to time, for activities and/or holdings in corporations.

2. The Governor of the Bank of Israel has permitted the Bank, by virtue of his authority under section 31 of the Banking (Licensing) Law, 1981, to hold the means of control of overseas corporations (hereinafter: "the overseas corporations"), and by virtue of this permit, the Supervisor of Banks has approved holdings by the overseas corporations in other corporations ("sub-subsidiaries"). In addition, there are specific approvals relating to sub-subsidiaries. The permit for the holdings in the overseas corporations was issued on 23 February 2006 in lieu of previous permits, and such permit was given subject to the Bank acting to implement the requirements of the Supervisor regarding supervision and control of the overseas corporations and the sub-subsidiaries. The permit of the Supervisor to hold the means of control in overseas corporations and the Supervisor's approval to hold overseas corporations in sub-subsidiaries were amended in November 2011, enabling the Bank to hold 100% of the means of control of Banque Safdié S.A. and its subsidiaries, for the purpose of its merger into Leumi Switzerland (which thereafter changed its name to Leumi Private Bank).

The corporations included in the Governor's permit are: Bank Leumi USA, Bank Leumi (Switzerland), Bank Leumi (UK), Leumi (Latin America), Bank Leumi (Luxembourg), Bank Leumi (Jersey) and Bank Leumi Romania.

The permit is subject to a number of conditions regarding levels of holdings; supervision, control and monitoring of the management of the overseas corporations and sub-subsidiaries; the requirement for approval, a report, or notification to the Supervisor regarding various events, such as: investments in corporations, significant new activities, the opening of a branch or representative office; and the giving of information and documents to the Supervisor.

3. With regard to restrictions imposed on the depositing of monies between Group companies, see above in the chapter, "Business Description of Leumi Group and their Economic Development"

Material Agreements

1. Following publication of the circular by the Supervisor of Banks regarding measurement and disclosure of impaired debts, credit, and the allowance for credit losses, (hereinafter "Directive of the Bank of Israel"), the banks, including the Bank, reached an agreement with the Tax Authority regarding recognition of allowances for credit losses for tax purposes.
The agreement was signed on 19 March 2012, and is effective for impaired debts that were recorded from 1 January 2011 onwards.

This agreement replaces the earlier agreement which applied to doubtful debts recorded through 31 December 2010.

The main points of the new agreement are as follows:

Large impaired debts on an individual basis:

The allowance is recognized as tax deductible in the same year it is recorded as an expense in the financial statements. In the tax year in which the balance of the allowance for credit losses was reduced (not as a result of an "accounting write-off" or a "waiver"), an "additional tax" will be added to the Bank's tax liability, with the addition of interest and linkage differentials, which will result in a tax charge which would have been collected if the allowance permitted to be deducted had not been recognized at the outset.

For this purpose – a "large debt" is a debt of NIS 1 million or more, or a lower amount as notified by the Bank to the assessing officer and in accordance with the Bank's characteristics.

Impaired debts that are not large:

The expenses in respect of a net "accounting write-off" (after offsetting tax payment for the same year) – half are recognized for tax purposes in the first tax year following the year in which the expense was recorded, and half are recognized in the subsequent tax year in which the expense was recorded.

Collective allowance:

This is not recognized for tax purposes.

Allowances in respect of "retail debts" recorded up to 31 December 2010:

These will be recognized as tax deductible in five annual equal installments, beginning in 2011, providing they were not recognized as an expense for tax purposes in previous years.

Implications of the initial implementation of the Bank of Israel's directive on 1 January 2011:

Differences deducted from shareholders' equity as a result of the initial implementation of the Bank of Israel's directive will be recognized as tax deductible in five annual equal payments, beginning tax year 2011, subject to their being recognized for tax purposes in accordance with the terms of the arrangement, and on condition that they are not collective, general or supplementary provisions.

2. A compromise agreement for the regulation of tax payments in Israel in respect of profits of subsidiaries of the Bank overseas, between the Bank and the Assessing Officer for Large Enterprises of August 1987, which was extended in October 1991 until the end of 1993, and again in March 1994, when its term was extended until such time as one of the parties gives a year's notice of its intention to propose changes to the agreement.

3. An agreement from April 2005 between the Bank and the Tax Authority in connection with an offset in respect of the profits of a foreign subsidiary.

For further details, see Note 26(I)

4. An agreement between the Bank and Union Bank Ltd. ("Union Bank") for providing comprehensive computing and operational services, including development work and new and special projects as well as relevant training, by the Bank to Union Bank and its related entities, signed in September 2001 and effective retroactively from September 1998 for a period of 11 years with an extension option. In December 2007, an addition to the agreement was signed by Leumi and Union Bank, concerning an extension of the relationship, with changes in the business terms. The new relationship term is ten years, starting from 1 January 2007, during which a gradually increasing annual consideration will be paid to the Bank, starting at some NIS 40 million in the first two years and up to some NIS 45 million starting from the sixth year (the sums are linked to the December 2006 CPI, and are contingent upon Union Bank's volume of activity). The addition was approved by the Supervisor of Banks and the Antitrust Commissioner.

   In December 2013, Union Bank announced that, pursuant to its right according to the agreement, it was postponing the commencement of the project of terminating the engagement with the Bank (as this term is defined in the agreement), such that it will begin at the end of the period of the agreement (31 December 2016). This postponement does not constitute a determination in relation to the question of renewing the agreement between the parties.

5. Pursuant to a decision of the Government, it was decided to establish Government Interior Fund as part of the Tax Authority (hereinafter – the Fund), which will undertake to pay a banking corporation an amount amounting to the VAT component, out of the summary paid by the banking corporation to the purchaser of an apartment, due to the forfeiture of a bank guarantee made by the banking corporation to that purchaser pursuant to the Sale Law (Apartments) (Guarantee of Investments of Purchasers of Apartments), 1974. The terms of the Fund's undertaking to pay the VAT component are set forth in the liability note signed by representatives of the Tax Authority and the Accountant-General, together with the approval of the banking corporation wishing to join the arrangement.

   Bank Leumi Le'Israel intends to sign the liability note.

6. Letters of Indemnity as detailed in note 18G to the financial statements.

Description of the Taxation Position

1. **(a)** On 13 August 1987, a compromise agreement was signed between the Bank and the Assessing Officer for Large Enterprises, which regulates tax payments in Israel in respect of profits of overseas subsidiaries of the Bank, pursuant to which from 1978 and thereafter the Bank's share of the profits of overseas subsidiaries on a consolidated basis will be included in the Bank's assessment. The agreement provides that it does not determine that the companies owe tax in Israel or that Israeli law applies to them and that the agreement does not constitute a precedent. The agreement was extended on 10 October 1991 with effect until the end of 1993, and again on 13 March 1994 and it will be in force until one of the parties gives a year's notice of its intention to propose changes to the agreement.

(b) Pursuant to an arrangement with the tax authorities dated 14 April 2005, as from 2004, the Bank may set off from its tax liability in Israel, in respect of the profits of an overseas subsidiary, an aggregate amount of up to US$ 67 million, but no more than the lower of US$ 3 million a year or the tax liability in Israel.

2. Amendment No. 11 to the Income Tax (Adjustments by Reason of Inflation) Law, 1985, provided that, *inter alia*, all the assessed parties to whom the amendment applies must pay tax on profits from securities traded on an exchange at the time of realization. The Amendment came into force in 1999. In the opinion of the tax authorities and the banks, taxing securities on a realization basis does not accord with the nature of the financial institutions' activity.

In light of this, on 6 June 1999, the tax authorities sent the banks a draft proposal to amend section 6 of the said Law, pursuant whereto the financial institutions would be taxed on the basis of the increase in the value of the securities, in accordance with the manner of presenting securities in the financial institutions' financial statements.

In coordination with the tax authorities, the Bank operates on the basis of the draft proposed law, and the tax provisions were made accordingly.

3. On 28 May 2013, the Finance Minister signed an order raising the rate of value added tax in respect of transactions and the import of goods from 17% to 18%, with effect from 2 June 2013.

On 2 June 2013, the Value Added Tax Order (Rate of Tax on Non-Profit Associations and Financial Institutions) (Amendment), 2013 was published, updating the rate of profit tax and salary tax imposed on financial institutions from 17% to 18%. As a result of the said change, the statutory rate of tax applicable to financial institutions increased in 2013 from 35.9% to 36.21%. Furthermore, the rate of salary tax applicable to financial institutions increased from 17% to 18% with respect to the salary payable for work in June 2013 and onwards.

The change in the rate of profit tax has led to an increase in net balances of deferred tax receivables amounting to NIS 30 million in the second quarter of 2013. The effect of the increase in salary tax on the balance of liabilities to employees as at 30 June 2013 is NIS 53 million before tax and NIS 34 million after tax. The change in salary tax led to an increase of NIS 56 million in current salary expenses and operating expenses in 2013, compared to 2012.

On 30 July 2013, the Economic Plan for 2013-2014 (The Budget Law) was approved in the Knesset plenum, including *inter alia*, an increase in the company tax rate from 25% to 26.5% with effect from 1 January 2014.

The change in the company tax rate and the change in the rate of profit tax, mentioned above, will raise the statutory tax rate which applies to financial institutions from 36.21% in 2013 to 37.71% in 2014 and thereafter. The change in the company tax rate led to an increase of NIS 107 million in the net deferred taxes balances receivable.

On 13 August 2012, the Deficit Reduction and Change in Tax Burden Law (Legislative Amendment), 2012 (hereinafter: "the Law") was published. Pursuant to the Law, with effect from January 2013, the rate of National Insurance premiums collected from employers in respect of the part of the salary exceeding 60% of the average salary in the economy increased from 5.9% to 6.5%. In addition, it was provided that this rate would increase in January 2014 and January 2015 to 7% and 7.5%, respectively. However, on 27 January 2014, the Reliefs in the Capital Market and Encouragement of Activity Therein Law (Legislative Amendments), 2014, was published, according to which the rate of insurance fees collected from employers in respect of the part of the salary exceeding 60% of the average salary in the economy would be updated in January 2014, January 2015 and January 2016 to 6.75%, 7.25% and 7.5%, respectively.

The current taxes for the periods reported in these financial statements are calculated at the tax rates as determined in the laws referred to above.

The balance of the deferred taxes to 31 December 2013 were calculated at the tax rate as determined in the laws referred to above, at the tax rates at the expected date of reversal.

For further details regarding the policy for recording deferred taxes in the Bank, see Note 1(S).

4. The Bank has been issued with final assessments for the period up to and including the 2007 tax year. The principal consolidated companies have issued final assessments up to and including the 2009 tax year.

Further details regarding the tax provision of the Bank and its subsidiaries, final assessments, carryforward tax losses and differences between the statutory tax rate and the effective tax rate, see Note 26 to the financial statements.

Human Resources

Number of Personnel

In 2013, the number of positions* in the Group decreased by 403, a fall of some 3.0% in relation to the number of positions in 2012. With regard to the average for the year, the number of positions in the Group fell by 259, a fall of some 1.9% in relation to the average for 2012.

This fall derives from streamlining procedures in the number of positions in the Bank due to making a structural change in the activity of branches in the offices and streamlining procedures in the subsidiaries in Israel and abroad. The gap between the rate of specific decrease in the number of personnel and the rate of the average decrease derives from an acceleration of the leaving rate towards the end of the year.

	Positions at year end		Average positions during the year	
	2013	2012	**2013**	2012
The Bank in Israel	**9,785**	10,154	**10,088**	10,265
Consolidated subsidiaries in Israel	**2,038**	2,057	**2,023**	2,053
Total of the Group in Israel	**11,823**	12,211	**12,111**	12,318
Overseas: Bank branches and representative offices	**45**	49	**47**	49
Consolidated subsidiaries	**1,136**	1,147	**1,149**	1,199
Group total in Israel and overseas	**13,004**	13,407	**13,307**	13,566

* Position – means a full time position including specific overtime, working hours of employees from temporary employment agencies and employment of external consultants.

Streamlining program and early retirement

As part of preparations for the 2012 work program, it was decided to embark on an efficiency program affecting 800 positions over a period of three years until the end of 2014.

The program was based mainly on the "Advancing Together" project which advances the transfer of back-office activity from the branches to centers of expertise and a streamlining project in the divisions' staff; which included, *inter alia*, streamlining in the Private Banking Department, the merger of Leumi Mortgage Bank and the merger of the Corporate Division and the Commercial Department. The program was originally based on levels of expected natural retirement; and a reduction in the level of recruitment, at the same time, utilizing the potential of the existing human capital.

During 2012, with progress in the streamlining process, after further consideration, it was decided to change the quality mix of the workforce in the program and, to this end, directing efforts towards the early retirement of veteran employees. In view of this, a provision of NIS 323 million was made for financing early retirement. With the progress of the streamlining measures and the acceleration of the rate of early voluntary retirements, it was decided to increase the original streamlining target from 800 positions to 900, and consequently, an additional sum of NIS 75 million was provided to finance the additional retirement.

During 2013, the streamlining measures and process of early retirement continued. From the beginning of the retirement procedures to 31 December 2013, 433 employees signed for early retirement, most as part of structural change.

Natural retirement

During 2013, around 100 employees left the Bank by natural retirement.

Over the coming decade, around 2,200 employees are expected to leave by natural retirement, of which 119 employees, in 2014.

Remuneration system and salary structure

In general, the salary and remuneration systems for the Bank’s employees are based upon a correlation between the level of remuneration and the position of the employee, the contribution of the employee to the Bank and the evaluation of the employee’s manager. Consequently, the remuneration granted to the employee is differential.

Collective agreements with the employees

In 2013, no collective agreements were signed.

For details in connection with the remuneration of senior officeholders, see chapter, "Remuneration of Senior Officeholders"

Labor and Salary Costs (in the Bank)

	2013 **	2012	2011
	NIS thousands		
Cost per employee position (excluding bonus)*	**339.2**	330.3	316.7
Cost per employee position (including bonus)*	**368.0**	331.2	323.3
Salary per employee position (excluding bonus)*	**222.4**	219.6	211.8
Salary per employee position (including bonus)*	**245.4**	220.2	217.2

* Cost per employee position does not include pension expenses, costs of voluntary retirement, retro-severance pay and shares to employees.

** In 2013, the data include the effect of the cost of employees from the Mortgage Department which was merged with the Bank.

Training and Development

The Management of the Bank sets itself the goal of supporting the business units and the attainment of their business goals through study and training procedures, which focus on improving the professional and managerial ability of employees and managers. In this context, Leumi employees participated in 46,178 training days during 2013.

Training activities in 2013 focused on raising the level of professionalism of the employees with emphasis on core banking areas – credit, investment counseling, service and sales and management training, all according to the business objectives of the Bank, including comprehensive training and assimilation with regard to regulations and compliance for all the Bank's employees.

Digital learning

In 2013, the remote-learning by video (LM) became a part of the learning culture in Leumi in general, and in the Banking Division, in particular, with the intention of keeping the high level of skill of employees, while making significant saving on travels and the loss of business time. As support for this trend, designated learning stages were allocated to branches and video sets were distributed to most segment managers.

Manager development

Implementation of the manager development program at Leumi continued in 2013, and during the year, most managers participated in one of the following frameworks: management courses, professional courses, business-support activities, skill development programs and training at various levels. In addition, development programs were carried out for managers participating in the Bank's management cadres.

Education

The percentage of employees with university education at the Bank has been on a continuing upward trend.

The percentage of university graduates at the Bank was 66.4% of all employees at the end of 2013, compared with 64.6% in 2012, 63.5% in 2011 and 61.4% in 2010. The percentage of graduates among the managerial staff reached 94.4% in 2013, in comparison with 93.4% in 2012, 93.0% in 2011 and 92.6% in 2010.

This increase in the percentage of university graduates is the result of the recruitment of employees with university education, the resignation of Bank employees who were not university graduates, and the acquisition of higher education by Bank employees.

Employee Rights

Labor relations between the Bank and its employees in Israel, save for those with personal employment contracts, are primarily based upon a basic collective labor agreement known as the "Labor Constitution" and supplementary and collective agreements. The terms of employment of members of the Bank's Management and certain other senior employees are regulated by personal employment contracts. For additional details see note 15 to the financial statements.

Organizational Culture

In 2005, Leumi launched the ethical code "the Leumi Way".

In 2013, a process of examination and strategic thinking was carried out in the Bank management, and consequently, the Group's vision was crystallized, core values and strategic goals were examined and reformulated and the ethical code was updated.

The new vision is "*Leading proactive and innovative banking for the customer*" and the new core values are: "*The customers are the core activity. Yes, we can - collaboration, personal example and excellence*!"

The vision and new core values will be launched as part of the divisional work program seminars and the balance sheet conference and will be assimilated through Bank-wide processes led by the heads of the divisions and departments. At the same time, they will continue to operate the ethical institutions: the Ethics Officer, the Ethics Centre, the Inter-divisional Ethics Committee and Divisional Ethics Committee.

In addition, the subject will continue to be examined within the framework of the SOX and Ma'ala's rating and will be a part of Leumi's Corporate Responsibility Report.

Employee involvement in the community

Leumi management views the involvement of its employees and managers in the community as a central goal of the Bank in the area of social responsibility. Leumi encourages its employees to take an active part in volunteer projects and to become involved in community life, and provides them with frameworks for volunteering and a variety of opportunities to contribute and volunteer.

During the course of 2013, some 3,754 employees – from various units within the Bank - engaged in volunteering activity. The total hours of volunteer work by employees from which the community benefited in 2013 was 30,904.

The activities of the unit are based on a network of social leaders in all the divisions and departments of the Bank, numbering some 320 employees representing the various units of the Bank. Their purpose is to promote the subject of volunteer work among employees in their unit while building an infrastructure to support the activity.

Leumi has a wide range of community partners, mainly in the area of children and young people. Many thousands of people every year benefit from the direct impact of volunteer work by Leumi employees.

Employees from throughout the country are involved in a range of activities such as assisting children and youth at-risk in residential homes, clubs and community centers; tutoring, assisting with homework and accompanying youth groups, collecting equipment for the needy, visiting hospitals, assisting Holocaust survivors, supporting populations with special needs, etc. Bank employees participate in the annual traditional Passover food collection, distributing meals to over 2,000 needy families. In 2013, a food distribution campaign for needy families took place marking the Ramadan festival.

Alongside these many activities, Leumi chose to link with Leumi's vision of strengthening the future generation, through strategic programs, such as "Leumi On the Move" program in partnership with youth movements, strengthening the connection with associations supported by the "Leumi Tomorrow" organization with various projects, such as "Youth Leading Change". In the past year, Leumi employees have integrated successfully in Project "Taglit", managed by the Jewish Agency, as well as other projects. In the involvement of Leumi employees in the community and the various interfaces with children and youth, care is taken with regard to the contents, including the assimilation of values and, gradually, the financial education matching the Bank's core business.

Positions according to operating segments:

	Average positions in 2013		Average positions in 2012	
	Managerial Staff	**Clerical Staff**	Managerial Staff	Clerical Staff
Households	**1,450**	**5,557**	1,472	5,697
Small businesses	**476**	**1,446**	483	1,364
Corporate banking	**429**	**605**	439	664
Commercial banking	**769**	**1,075**	779	1,120
Private banking	**419**	**387**	454	421
Financial management – capital markets	**313**	**369**	303	359
Other	**3**	**9**	2	9
Total	**3,859**	**9,448**	3,932	9,634

The calculation of the number of positions according to operational segments is based on the management of personnel according to the Bank's main lines of business, with various adjustments and on the basis of assessments. In calculating the number of positions according to operating segments, employees of head office units, who serve all or part of the operating segments of the Bank, have also been taken into account.

Appointments and Retirement

Appointments:

Professor Daniel Tsiddon, a member of Bank management, was appointed Head of the Capital Markets, Private Banking and Strategy Division, with effect from 1 April 2013.

Mr. Yaakov Haber, a member of Bank management, was appointed Head of Corporate Division with effect from 1 January 2013 and to the post of Head of the Corporate and Commercial Division, with effect from 1 January 2014.

Ms. Tamar Yassur was appointed to the post of Head of the Banking Division and member of Bank management and to the post of chairman of the board of directors of Leumi Card, with effect from 1 January 2013.

Mr. Dan Yerushalmi was appointed to the position of Head of Operations and Information Systems Division and member of Bank management, with effect from 1 March 2013. From 1 January 2013, and until he took up his position, Mr. Moshe Wolf acted in his place.

Mr. Shlomo Goldfarb was appointed to the position of Head of Accounting Division, Chief Accounting Officer and member of Bank management, with effect from 1 April 2013.

Mr. Itai Ben-Zeev was appointed to the position of Head of the Capital Market Division and member of Bank management, with effect from 1 April 2013.

Mr. Joel Mintz, a member of the Bank management and Head of the Structured Finance and Real Estate Division, was appointed Head of the International Credit and Real Estate, with effect from 1 January 2014.

Mr. Amir Lazar was appointed to the post of Head of the Mortgage Department, with effect from 1 January 2013.

Ms. Osnat Tennenbaum was appointed to the position of Head of the Special Credit Department, with effect from 1 February 2013.

Mr. Ehud Zilberberg was appointed to the position of General Manager of Leumi Switzerland, with effect from 1 July 2013.

Mr. Avner Mendelson, left his post as Head of the Strategy Department and the International Activity Staff and was appointed to the post of the General Manager of Leumi USA, with effect from 1 September 2013.

Mr. Shmuel Arbel was appointed to the post of Head of the Commercial Department with effect from 1 January 2014.

Mr. Shaul Schneider was appointed to the post of Head of the Private Banking Department with effect from 1 February 2014.

Mr. Zeev Morag was appointed to the post of Head of the Compliance and Enforcement Department and promoted to the rank of Deputy Vice-President with effect from 1 March 2014.

Retirements:

Mr. Menachem Schwartz left his position as Head of the Accounting Division and member of Bank management on 31 March 2013 and retired on 31 October 2013, after 43 years employment in the Bank.

Mr. Gildon Altman left his position as Head of the Commercial Banking Division and member of Bank management on 31 December 2013 and will retire in 2014, after 35 years employment in the Bank.

Mr. Amnon Zaidenberg left his position as General Manager of Leumi Switzerland on 30 June 2013.

Mr. Eyal Yitzhak left his position as General Manager of Leumi USA on 31 August 2013 and will retire in 2014 after 39 years in the Leumi Group.

Mr. Moshe Ingevir left his position as Head of the Special Credits Department on 31 January 2013 and retired after 46 years employment in the Bank.

Ms. Nitza Rousso–Stauber left her position as Head of the Private Banking Department on 31 January 2014 and retired after 13 years employment in the Bank.

Ms. Meira Karni left her position as Head of the Compliance and Enforcement Department on 28 February 2014 and will retire in 2014, after 32 years employment in the Bank.

Mr.Shlomo Pergament will leave his position as Deputy Head of the Operations and Computers Division on 5 May 2014, and will retire in 2014, after 36 years employment in the Bank.

Organizational Structure

The Leumi Group's organizational structure, according to lines of business and head-office services, as described below, combines the activity of companies in the fields of banking, finance, the capital market and financial services.

Lines of Business

Leumi is organized into five lines of business that focus on different market sectors, and each business line specializes in the provision of service to a group of customers. This form of organization enables the customers to enjoy a high standard of professional service, varied distribution channels, products that are adapted to their requirements and fast and flexible decision-making processes.

Following is a description of the responsibility for Leumi's five lines of business:

1. The **Banking Division** manages the activity of the private and small business customers, who receive the full range of services through 205 branches which are organized in 8 districts on a geographic basis and by means of a variety of technological/direct distribution channels, including Leumi Call, which provides services to customers through the telephone, cellular phones and the Internet. The services and products are adapted to all the customer sectors differentially according to the nature of their banking activity, their characteristics and their needs. The customers of the Division are segmented into the following sectors: the retail segment, the premium segment, and the corporate banking segment. The Division coordinates the retail operations in the Group, including those of the Arab Israel Bank and Leumi Card.

The **Mortgage Department –** From 31 December 2012**,** the Mortgage Department constitutes an independent unit within the Banking Division. Its main activity is in the sector for loans to purchase housing and in the sector for any-purpose loans with a housing mortgage, with specific skill and expertise in the area. The department operates through 109 representative offices, most of which are located in branches of the Banking Division, with a few in independent locations. The representative offices report to five regional areas which report to the department's management. The department operates a business center which coordinates activity in the area of credit, underwriting and the transfer of loan funds to customers. The department also operates telephone call-centers which allow the submission of requests for approval in principle of a credit facility via telephone and the Internet, and the provision of a qualitative service to existing borrowers regarding managed loans.

2. The **Corporate and Commercial Division** includes two departments, the Business Department and the Commercial Department (as detailed below), the Tel Aviv Central branch and head office units providing service to the whole Corporate and Commercial Division and the International Credit and Real Estate Division. The division is also responsible for activity planning special transactions, such as the finance of projects, transactions to finance the means of control, the organization of syndicates, the sale of debts, and the examination of investment plans, international trade and finance.

The **Corporate Department** manages the banking activity of the large business companies in the economy on the basis of sector expertise and synergy between industries. The department includes four business sectors: a technology sector, a sector for chemicals, energy and holding companies, a consumption and trade sector and a sector for industry, transport and institutions.

The **Commercial Department** manages the activity of middle-market commercial companies, through the Commercial Section in the main Tel Aviv branch and 23 business branches - organized on a geographical basis into 4 commercial districts. The Division's organizational structure is unique in the banking system, providing the customer with a "one stop shop" for its comprehensive and extensive services, while broadening its services to business customers through digital channels.

3. The **International Credit and Real Estate Division** manages the large building companies, promoters and contractors in the economy (including national infrastructure projects) with specific skill and expertise in all areas of real estate in the economy. The financial services are provided both to finance the activity of the customers in Israel through the Bank's branches, and to fund their activity abroad through the Bank's overseas units. The Division also includes the Special Loans Unit. In addition, the Division has responsibility in examining aspects of business credit in the Bank's overseas units in the United Kingdom, the United States and Romania.

   The **Special Loans Unit** which deals with corporate customers who are in difficulty, while attempting to assist in the recovery of active customers through business help and support and the collection of business customers' debts whose rehabilitation is not possible. In addition, the unit coordinates the professional assistance required for clarifying demands and claims against the Bank and the consulting for the entire Bank on topics related to its area of expertise.

4. The **Capital Markets Division** is responsible for managing the Group's financial assets in Israeli currency and foreign exchange; management of the *nostro*; the activity of all the Bank's dealing rooms (Israeli currency, foreign exchange and Israeli and foreign securities); developing innovative financial products and investment products; management of the assets and liabilities of the Bank and management of market risks; management of the formulation of a price policy and financial margins in the Bank; relations with financial institutions abroad; co-ordination of the Bank's capital market operational services; and operational service for customers active in the capital and financial markets, including institutional customers.

5. The **Private Banking Department** is responsible for the private banking activity in the Group in Israel and worldwide. The department has 7 private banking centers in Israel for residents and non-residents and is also responsible for the activity of Bank Leumi le-Israel Trust Company Ltd. The department's activities also include, *inter alia*, control and co-ordination between the Bank in Israel and the overseas units dealing with private banking and establishing standards at an international level for the provision of service to wealthy customers of the Group.

As well as the division according to line of business, Leumi Group has the following head office units which provide services to the business units:

The **Finance and Economics Division** is responsible for coordinating and preparing the Bank's work-plan; managing profit centers and financial and managerial measurement; planning and managing the Group's capital; preparing the Bank's expenditure budget and monitoring its application, sharing in the determination of the order of priorities in the investment budget, coordination of commissions policy, managing the Bank's and the Group's tax matters and the Bank's and the Group's insurance, connections with investors and analysts, monitoring economic developments and preparation of sectoral reviews and economic forecasts, the formulation of concepts, processes and organizational and administrative solutions, the formulation of models for optimization of resources and the direction of overseas units and the analysis of their activity.

The **Procurement, Construction and Logistics Department** is a part of the Finance and Economics Division and is responsible for providing services in the area of procurement (general, construction and technological), construction and maintenance, asset management and the provision of various logistical services in the areas of consignment and management of a logistical center, in the Bank and in the subsidiaries in Israel.

The **Accounting Division** is responsible for managing, developing and determining the Bank's accounting guidelines, managing the Bank's books of account, preparing the financial statements of the Bank and the Group, the relationship with the Bank of Israel in all accounting matters and the related reports, and the monitoring of regulatory changes related to accounting and their assimilation in the Bank and in the Group. In addition, the Accounting Division is responsible for assessing the effectiveness of the key controls of the SOX 404 working process, calculating capital adequacy and reporting to the public in accordance with Basel II directives. From 1 April 2013, the Accounting Division reports to the Finance and Economics Division.

The **Human Resources Division** is responsible for the formulation and implementation of the Bank's human resources policy and, within this overall context, for selection and placement of employees, remuneration, salary structure, labor relations, development and advancement of employees, banking training – managerial and general, assimilation of the "Leumi Way" code of ethics, intra-organizational communications, internal information, care of the individual, organizational counseling and development, employee involvement in the community and employee welfare.

The **Investment Counseling Department**, which reports to the Human Resources Division, is responsible for Bank's policy regarding counseling in investments in securities, in financial instruments and in pension products, conducting research into capital market and finance matters, professional development for investment and pension consultants, the characterization of systems in the area of consulting and the development of management-supporting models, dealing with aspects of regulation in the area of investment and pension consulting and the adaptation of work procedures and rules in these areas to the directives of the regulator.

The **Operations, Information Systems and Administration Division (*Chatam*)** is responsible for the computerized and operational deployment of the Bank and the Group. As part of its task, the Division co-ordinates the formulation and determination of the strategy, policy and activity regarding technological development, computers, operations, data technology, communications, information security, operations of subsidiaries in Israel, and also support of the overseas units in all matters related to technological services, operation and the receipt of assistance required from Bank Leumi in Israel, and extending automated solutions required for achieving Leumi's business goals.

The **Legal Division** is responsible for overall legal counsel to the Bank and its subsidiaries in Israel and the management of legal risks in the Bank and the Group. It is also responsible for expressing an opinion on various legal matters and for the infrastructure of legal forms and opinions, following legislative and regulatory proceedings and representation of the Group with the various legislative and regulatory bodies, legal advice for new products developed or integrated in the activity of the Bank and Group, and is responsible for dealing with claims against the Bank, the employment of outside attorneys and their supervision.

The **Internal Audit Division** is responsible for the internal auditing of the Leumi Group. The Audit Division operates by virtue of the Internal Audit Law – 1992, Proper Conduct of Banking Business Directives of the Bank of Israel and directives of the Board of Directors. In addition, the Division acts in accordance with professional standards of the Institute of Internal Auditors.

The division deals, in an independent, impartial manner, with the examination and assessment of the Group's internal control system, including: examination of the work and control processes, examination of the method of managing various risks in the Group, maintenance of the Bank's assets, minimization of exposures, compliance with the rules of ethics and proper governance, implementation of the directives of the Board of Directors, the management and the Bank's procedures, and the examination of operational efficiency. In addition, the Audit Division conducts an independent review of the internal process for an assessment of capital adequacy of the Group (ICAAP). The Chief Internal Auditor is directly responsible to the Chairman of the Board of Directors.

The **Risk Management Division** is responsible for risk management in the Group and in the Bank, and coordinates risk management at the Group level in the main risk areas: credit, market and operations and compliance. The Division operates with an emphasis on independence in risk-taking. The object of the Division is the creation of a strong infrastructure for managing and controlling risks that will support the achievement of business targets, in accordance with the defined risk appetite. In addition, the Division is responsible for assisting the Board of Directors in defining the risk appetite, leading risk policy, developing and defining tools for measuring and pricing risks in the various activities; identifying, measuring and controlling the major risk focal points in the Group, and the changes occurring in them, and examining the risks inherent in new activities. The Division also includes the Credit Risk Management Units, which are responsible for the analysis of specific loans in excess of NIS 25 million and the Compliance and Enforcement Department.

The **Compliance and Enforcement Unit** is responsible for implementing compliance in the Bank and Group in relation to consumer regulations, including the prohibition on money laundering, the prohibition of the financing of terrorism, administrative enforcement and American customers (in conjunction with the Finance and Economics Division and the Legal Division).

The **Credit Risk Management Department** is responsible for the specific analysis of credit risk in excess of NIS 25 million, and for the examination of appropriateness of the classifications and allowances for credit losses. The Department is split into three sections: analysis of corporate credit risk, analysis of credit risk in the real estate sector and commercial credit risk. The analysis of the risks is achieved as part of the process of approving the credit and is presented to the relevant credit committee before making the decisions.

The **Marketing Department** is responsible for Bank and Group marketing and marketing communications, the spokesperson's office, regulation and public relations, conventions and events, marketing research, social media and sponsorships. Among other things, the Department is responsible for delineating Leumi's marketing strategy to advertise through the various media outlets, to create ties with the varied types of communication and media, and to manage government and regulation connections with the legislature and representatives of the State authorities. The Department administers the Group's sponsorship activity and is responsible for organizing conferences and events, for the Bank's employees and customers.

The **Strategy Section** is responsible for assisting Group Management and the Board of Directors in defining and planning Bank and Group strategy and its validation, examining and analyzing subjects with strategic implications, and providing support and leadership of main projects in cooperation with the lines of business.

During the year, a number of significant organizational changes were made in Leumi:

Capital Markets, Private Banking and Strategy Division

On 1 April 2013, Professor Danny Tsiddon, Deputy Chief Executive Officer, was appointed to the post of Head of the Capital Markets, Private Banking and Strategy, and the Head of the Capital Markets Division, Head of the Private Banking Department and the Head of the Strategy Section will report thereto.

Accounting Division

On 1 April 2013, a organizational change in structure was made in which it was decided that the Head of the Accounting Division, Mr. Shlomo Goldfarb would report to the Head of the Finance and Economics Division, Mr. Ron Fainaro.

Corporate and Commercial Division

On 1 January 2014, an organization structural change was made pursuant to which the Corporate Division and the Commercial Division were consolidated into one division, headed Mr. Kobi Haber, to whom the Head of the Corporate Department, the Head of the Commercial Department and the Manager of the Tel Aviv Central branch will report**.**

International Credit and Real Estate Division

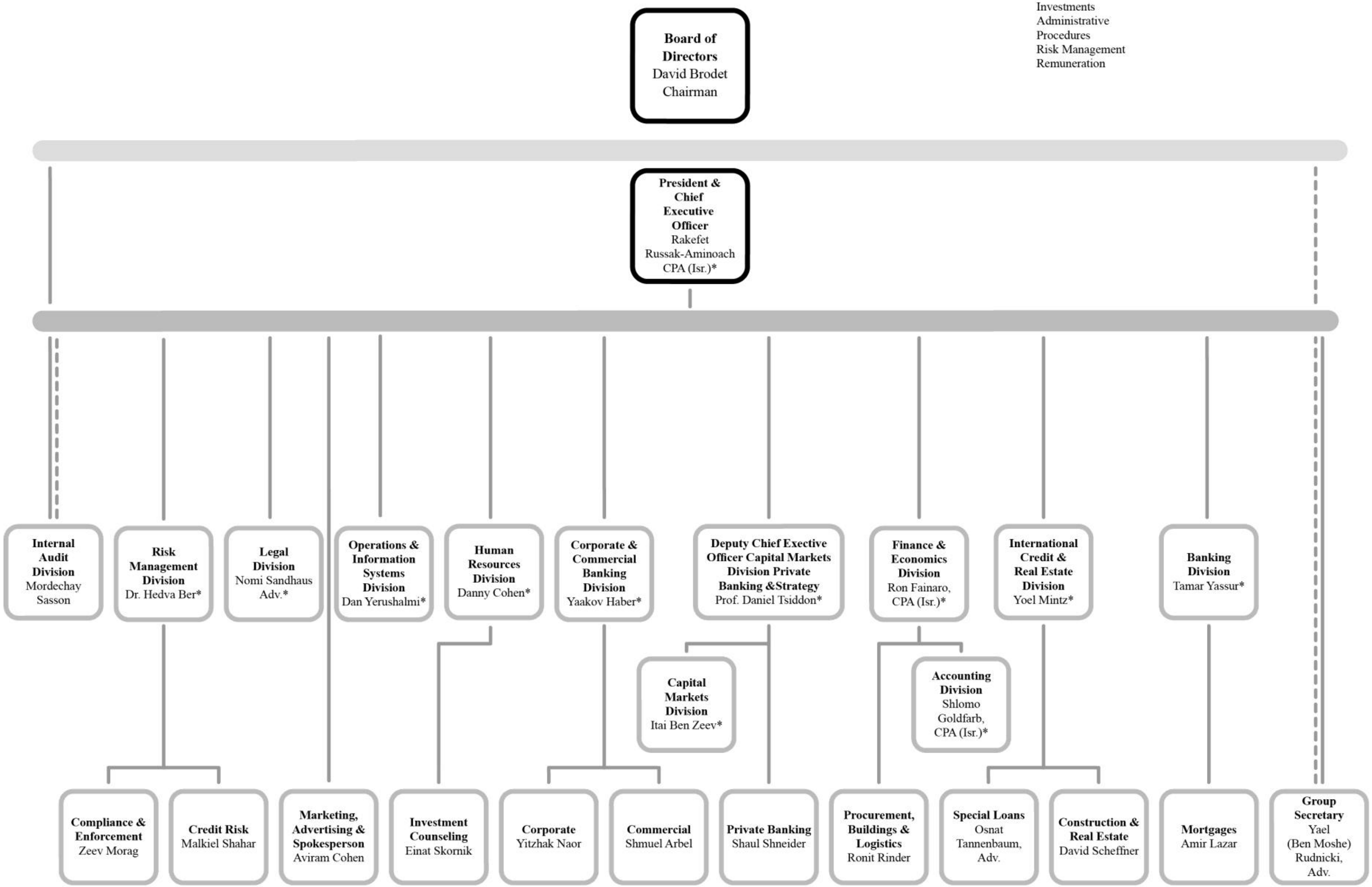
On 1 January 2014, as part of the organizational structural change in Corporate Division, it was decided that Mr. Joel Mintz, would report directly to the President and CEO and would receive responsibility for international credit in the Group, and that the Head of Construction and Real Estate Department and the Head of the Special Loans Unit would report thereto.

Risk Management Division

On 1 January 2014, with the aim of complying with the Bank of Israel Regulations (Proper Conduct of Banking Business Management Regulation no. 311), an organizational structural change was made, pursuant to which it was decided that the Credit Risk Management Department, headed by Mr. Malkiel Shahar, would be transferred to the responsibility of the Risk Management Division and will include the corporate, commercial and real estate credit risk management units.

Bank Leumi le-Israel B.M.
Organizational Structure

Committees of the Board of Directors
Credit
Strategy
Audit
Investments
Administrative
Procedures
Risk Management
Remuneration



* Member of Management

E. Additional Matters

Leumi for the Community – Social Involvement

Corporate responsibility management

The area of corporate responsibility in Leumi is managed on a basis of overall perception, strategy and policy led by the Board of Directors, and through various committees operating to advance the various topics: ethics, the environment, accessibility and community ties.

In 2013, the Leumi Group published its fourth corporate responsibility report, for the year 2011-2012, including a report on the diverse activities, initiatives, and achievements of the Leumi Group in the area of socio-environmental responsibility. The complete Corporate Responsibility Report appears on the Bank's website – plus.leumi.co.il.

The *Ma'ala* rating of corporate responsibility for 2013, published in June, again placed Leumi in the highest rated group (Platinum +).

Management of community ties

Leumi's social commitment is reflected in its constant investment in tomorrow's generation and the provision of opportunities and tools for its success. Leumi has chosen to focus on advancing education, culture and the arts, as well as activities that help close the gaps between the center of the country and the periphery. Leumi's social involvement is implemented via three main channels: "Leumi Tomorrow - The Centennial Fund for Endowing Israel’s Future Generation" (R.A), donations and financial sponsorships of social causes and volunteering activities of employees.

"Leumi Tomorrow - The Centennial Fund for Endowing Israel’s Future Generation"

The association invests in the advancement of youth by supporting various educational programs, operated by 12 social bodies and associations, among a range of population sectors throughout Israel. In 2013, the association donated NIS 12 million to various educational programs throughout Israel, in which more than 20,000 youth participated.

Alongside the monetary support, the social bodies and associations are able to participate in organizational workshops and financial conduct workshops given by Leumi employees on a voluntary basis, enjoy a manager tutoring program (mentoring) given by managers in the Bank, make use of the Bank's infrastructures and take part in a social partner forum, intended to develop the organizations' professional abilities.

In 2013, the "Leumi Tomorrow" program for matriculation preparation for Ethiopian immigrants, which operated from 2006 in conjunction with Tel Aviv University, came to an end. Support also finished for the "Partners For Life" program which was operated by the Keren Avraham Initiative Association, through which Arab women were trained for integration in the labor market. The success of the program led the Welfare Ministry to assume sponsorship, and it is now operated through other entities.

Other programs which Leumi contributes and sponsors

"Young Israeli Entrepreneurs" organization

Leumi is an involved partner in the "Young Israeli Entrepreneurs" organization, in which youth experience setting up a start-up company which advances a business idea of product development. Leumi's contribution to the organization focuses on assisting in the operation of the program in the social and geographic outlying areas, and the adoption of the program by branches of the Bank throughout Israel, and recruiting volunteer mentors from among employees of the Group.

The "Turning-Point" Program in cooperation with the Buchmann-Mehta School of Music at Tel Aviv University, and the Israel Philharmonic Orchestra.

In 2013, Leumi continued its support of the program, together with the Arab Israeli Bank of the Leumi Group. The program promotes artistic musical activity within Arab society, as well as joint activities with students on the campus of the Buchmann-Mehta School of Music**.** Reciprocal relations with the students at Tel Aviv University will create opportunities for connecting the center of the country with the outlying areas, as well as for bringing Jews and Arabs together.

The Leumi Center for Robotics

In order to encourage and promote excellence in science, and as part of its support of the future generation, Leumi contributed to the establishment of the Center for Robotics, and has sponsored the center's activities since 2009. The center's aim is to nurture motivation among the youth to engage in the fields of science, mathematics and technology.

Promotion of Israeli Creativity

As part of its responsibility for promoting and cultivating tomorrow's generation, Leumi initiates and supports ventures which allow young artists to exhibit their creations to the wider public. In addition, Leumi sponsors various exhibitions and cultural events.
In 2013, Mani House, Leumi's Visitors and Arts Center, which is open to the public, hosted three exhibitions displaying works by a number of Israeli artists. In addition, Leumi supported two unique exhibitions in areas outside Central Israel: "Spaces in the South" Exhibition in Sderot and "Colors of the Galilee" in Hatzor Hagelilit" which enabled residents of the areas to enjoy the finest current art.

Summary of Leumi's Donations and Sponsorships in 2013

In 2013, the Leumi Group made donations and provided sponsorships for social and community purposes in the amount of some NIS 25.6 million, of which donations amounted to some NIS 20.3 million.

Set out below is a breakdown by category of total donations and sponsorships in 2013:

Education, children and youth	- NIS 14.2 million
Culture and art	- NIS 3.1 million
Community and society	- NIS 6.2 million
Health	- NIS 2.1 million

Decisions regarding the designation and amount of donations are made, where applicable, by the Bank’s Donations Committee, the members of which are appointed by the President and Chief Executive Officer, and the "Leumi Tomorrow" voluntary association. Applications for donations are given careful and thorough consideration in accordance with criteria determined in the Bank’s donation guidelines and approved by the Board of Directors. Large donations (exceeding NIS 250,000) are referred to the Board of Directors for approval.

Internal Auditor

The Chief Internal Auditor, Sasson Mordechay has served as the Chief Internal Auditor since 1 March 2011. His appointment was approved by the Bank's Audit Committee on 13 December 2010 and by the Board of Directors on 14 December 2010.

The Chief Internal Auditor meets the criteria of section 146(b) of the Companies Law, 1999 and the provisions of section 8 of the Internal Audit Law, 1992 (hereinafter "the Internal Audit Law") and the internal audit employees meet the criteria of the provisions of paragraphs 11 and 12 of the Proper Conduct of Banking Regulations no. 307 regarding the internal audit function, with effect therefrom.

The Chief Internal Auditor is a full-time employee of the Bank, with the status of a member of management. This is his sole occupation and he is responsible within the organization to the Chairman of the Board of Directors.

The Internal Audit Division has an annual work plan and a multi-year work plan for a period of up four years. The annual work plan and the multi-year work plan are derived from a mapping of audit subjects which are based, *inter alia*, on the documents detailed in Regulation 307. The work plans are derived from a systematic methodology of estimating risks and controls, according to which the frequency of the audit for each subject is established. Thus, regarding subjects with a higher level of risk, audits will be carried out once a year, while for subjects that involve a lower level of risk, audits will be carried out with a frequency of between two and four years. The proposed annual work plan and multi-year work plan are submitted by the Internal Audit Division and are approved by the Chairman of the Board of Directors, the Audit Committee and the plenum of the Board of Directors.

The Internal Audit Division's annual work plan and the multi-year work plan allow the Chief Internal Auditor to exercise discretion in deciding to deviate from the plan, as necessary.

In the context of the audit work, a sample of material transactions carried out by the Bank – including the procedures through which they were approved – are examined. For this purpose, material transactions include a material purchase or sale of activity, "transactions" - as stated in section 270 of the Companies Law and an "extraordinary transaction" – as defined in the Companies Law.

The Internal Audit Division's annual work plan and the multi-year work plan each include a chapter dealing with the annual and multi-year work plans of the material consolidated subsidiaries in Israel (as set forth in Note 6D to the financial statements). Employees of the Internal Audit Division serve as internal auditors of the Bank's consolidated subsidiaries in Israel. The process of structuring the consolidated companies' work plans is similar to the process of structuring the work plan of the Bank's Internal Audit Division. Generally, the financial statements of the companies included on equity basis include reference to the work plans of their internal auditors.

In the material foreign subsidiaries, a local internal auditor is appointed. The Internal Audit Division supervises the work of the local auditor, as provided in paragraph 21(L) of Regulation 307. This is carried out, *inter alia*, through an examination of the local internal audit working program abroad before it is presented for approval to the audit committee and the board of directors abroad. The Bank's internal work-plan includes targeted audits by the Internal Audit Division in Israel of the overseas subsidiaries, and the division of labor among the Israeli and overseas auditors. The internal auditors of the significant overseas subsidiaries report to the board of directors of their local audit committee.

The Chief Internal Auditor and his team of employees in the Leumi Group in Israel comprise, on average, 107.4 positions for 2013, as described below:

	Average positions of auditors in the Leumi Group in Israel
The Bank	93.1
Subsidiaries in Israel	9.7
Overseas subsidiaries	4.6
Total	107.4 *

(*) Of which 5 positions on average are maternity leave / unpaid vacation.

In addition, 2.1 positions were invested on an outsourcing basis.

Furthermore, local auditors are employed in overseas subsidiaries in 20.6 positions (including outsourcing).

The decrease in the number of positions in 2013 compared to 2012 is a part of the economic streamlining process in the Bank and a streamlining of working processes in the audit.

The number of positions was approved by the Audit Committee in Israel, based on the annual and the multi-year work plan.

The Chief Internal Auditor may, within the framework of the budget, use outsourcing for the execution of work that requires special knowledge or in the event of insufficient staff.

The table below shows details of the benefits and amounts which were paid or for which provisions were made for 2013 to the Chief Internal Auditor: (NIS thousands)

2013										
Holding in the capital of the Bank	Remuneration for services				Other remuneration		Loans given on beneficial terms			
	Salary	Bonuses**	Social benefit provisions	Share-based payments	Value of the benefit	Total *	Balance as at 31 December 2013	Average period until maturity (years)	Benefit provided over the year	Loans granted on regular terms
	NIS thousands									
0.003	**1,137**	**477**	**(29)**	**349**	**117**	**2,051**	**50**	**1.42**	**2**	**-**

* Excluding salary tax.
** Estimate – see Note 15G of the financial statements.

The total payments to the Chief Internal Auditor and the components thereof are submitted to and approved by the Audit Committee.

The Board of Directors believes that the holding of securities by the Chief Internal Auditor and the remuneration paid to him do not affect the exercise of his professional discretion.

The Chief Internal Auditor operates in accordance with the professional standards of the Institute of Internal Auditors in Israel and the international Institute of Internal Auditors (IIA).

In addition, the Chief Internal Auditor operates in accordance with the directives and instructions of the Supervisor of Banks, including Proper Conduct of Banking Business Regulation no. 307 regarding the internal audit function.

The Audit Committee and the Board of Directors have noted that in the Chief Internal Auditor's written declaration he complies with the requirements laid down in the abovementioned generally accepted professional standards, and he operates in accordance with the directives and instructions of the Supervisor of Banks. On the basis of this declaration, and on the basis of his role as expressed at the meeting of the Audit Committee of the Board of Directors, the Audit Committee and the Board of Directors are satisfied that the Chief Internal Auditor meets all the said requirements.

Generally, upon the issue of written audit reports and records of the findings of the examination by the Internal Audit Division, and as part of the ongoing work process, discussions are held with the audited entities (branch managers, district managers or managers of other organizational units) on the audit reports and records, and discussions are also held on material findings with the heads of the divisions and the President and Chief Executive Officer.

Before the meetings of the Audit Committee, the Chairman of the Audit Committee, in consultation with the Chief Internal Auditor, determines which audit reports and records of the examination's findings will be presented in their entirety for discussion at the Audit Committee. Furthermore, lists of all the audit reports and records issued by the Internal Audit Division in the relevant period, together with a summary of the material findings, are submitted on an ongoing basis for the perusal of all the members of the Audit Committee. They may peruse any audit report they wish and make a request to the Chairman for them to be presented in their entirety for discussion by the Audit Committee.

Material audit reports and records of the examination's findings are discussed at the Audit Committee each month, and on occasion, several times a month.

At the end of the first and second halves of the year, the Internal Auditor submits to the Chairman of the Board of Directors, the President and Chief Executive Officer and the Chairman of the Audit Committee reports summarizing the audit operations. They include a summary of the material findings, the auditor's recommendations and the audited entity's replies for the relevant periods.

In addition, the Chief Internal Auditor submits to the Chairman of the Board of Directors, the President and Chief Executive Officer and the Chairman of the Audit Committee an annual report summarizing the audit operations during the course of the entire year, which also includes monitoring the performance of the annual work plan and an assessment of the effectiveness the Bank's internal control framework.

The work program of the Internal Audit Division for 2013 was submitted to the Audit Committee on 17 January 2013 and discussed in committee on 20 January 2013, and was submitted to the Board of Directors on 31January 2013 and approved in the Board of Directors on 3 February 2013.

Annual reports of the Israeli and overseas subsidiaries for 2012 were submitted to the Audit Committee on 22 April 2013 and discussed in the Committee on 25 April 2013.

The Internal Auditor's report for the first half of 2013 was submitted to the Audit Committee on 19 August 2013 and was discussed by the Committee on 22 August 2013.

The Internal Auditor's report for the second half of 2013 was submitted to the Audit Committee on 17 February 2014 and was discussed by the Committee on 20 February 2014.

The annual report of the Internal Auditor for 2013 was submitted to the Audit Committee on 17 February 2014 and was discussed by the Committee on 20 February 2014 and submitted to the Board of Directors on 6 March 2014 and will be discussed in the Board of Directors immediately prior to the publication date of the financial statements.

The work program of the Internal Audit Division for 2014 was submitted to the Audit Committee on 23 December 2013 and approved in the Committee on 26 December 2013, and submitted to the Board of Directors on 16 January 2014 and approved in the Board of Directors on 19 January 2014.

The Chief Internal Auditor has been provided with documents and information as specified in section 9 of the Internal Audit Law, and was given access to information, as specified in that section. He has continuous and direct access to the Bank's information systems, including access to financial data.

The internal auditors in Israel carrying out audits of the subsidiaries in Israel and abroad have been provided with documents and information as specified in section 9 of the Internal Audit Law, and were given access to information, as specified in that section. They have continuous and direct access to the information systems of the subsidiaries in Israel and abroad, including financial data.

The Board of Directors and the Audit Committee believe that the scope, nature and continuity of operations and the work plan of the Chief Internal Auditor are reasonable under the circumstances, and that they enable the Internal Audit in the Group to achieve its goals.

Disclosure Controls and Procedures for the Financial Statements

The directives of the Supervisor of Banks apply the requirements of Sections 302 and 404 of the SOX Act to banking corporations. With regard to these sections, the SEC and the Public Company Accounting Oversight Board have provided directives as to management's responsibility for the determination and existence of controls and procedures with regard to disclosure and existence of internal control over financial reporting and the external auditors' opinion with regard to the audit of the internal control over financial reporting.

The Supervisor's directives provide that:

- Banking corporations shall apply the requirements of Sections 302 and 404 and also the SEC's directives that were published by virtue thereof.
- 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 the requirements and can be used to assess the internal control.

The Bank implements the directives in the Leumi Group on a day-to-day basis.

In 2013, the Bank carried out a validation and update of material control processes and checks of the effectiveness of the entire internal control system on financial reporting.

Assessment of controls and procedures with regard to disclosure

The management of the Bank, together with the President and Chief Executive Officer, the Head of the Finance and Economics Division and the Chief Accounting Officer, has evaluated, as at the end of the period covered by this report, 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, the Head of the Finance and Economics Division and the Chief Accounting Officer 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 directives of the Supervisor of Banks on reporting to the public and at the time required in these directives.

Changes in internal control

During the quarter ended 31 December 2013, no material change to the internal control over financial reporting of the Bank occurred which had a material effect, or which could reasonably be expected to have a material effect, on the Bank's internal control over the financial reporting.

Remuneration Policy for Office-holders

On 11 February 2014, following the approval of the Board of Directors, pursuant to the approval and recommendations of the Remuneration Committee, the General Meeting of the Bank approved the remuneration policy for office-holders in the Bank in respect of the years 2013-2016. The remuneration policy is based on the provisions of Amendment 20 of the Companies Law with regard to the conditions of the term of office and employment of the office-holders in the Bank and the provisions of the new Proper Conduct of Banking Business Management Regulation 301A "Remuneration Policy in a Banking Corporation".

The remuneration policy is intended for the remuneration of office-holders in the Bank in accordance with the Bank's performances and profits over time, and in accordance with the Bank's and the Group's long-term targets, and the actual contribution of the office-holders to achieve these performances and targets. The remuneration policy includes, *inter alia*, consideration of the salary component, fringe benefits, retirement terms and the component of the annual bonuses.

For further details, see note 15 to the financial statements, below.

On 2 September 2013, the Bank received a letter from the Supervisor of Banks, requiring the Bank to postpone discussion regarding the remuneration of senior officers which was due to be held in the General Meeting called for 12 September 2013, and to hold it after the Supervisor of Banks completes the regulation of the new directive regarding the remuneration in a banking corporation. This postponement was intended, according to the Supervisor of Banks, to ensure that the Bank's remuneration policy would comply with the requirements which were to appear in the abovementioned new directive. In view of the Supervisor's demand mentioned above, on 3 September 2013, the Board of Directors decided to postpone the General Meeting which was called for 12 September 2013, as mentioned above. Attached to the Supervisor's letter was a clarification from the Israel Securities Authority (ISA) dated 28 August 2013, which stated that the ISA would not intervene in the postponement of general meetings for the approval of remuneration policy in accordance with Amendment 20 of the Companies Law beyond the last date provided for this in the said amendment, with companies being required to act until the approval of the remuneration policy, with regard to the approval of the terms of office and employment of all their officers, as companies that have yet to approve their remuneration policy. Also attached to the Supervisor's letter mentioned above was a letter from the Deputy Attorney-General dated 29 August 2013, reiterating the ISA's position outline above, and further clarified, among other things, that the postponement of the general meetings for a short period as required by the Supervisor does not adversely affect the interests of the shareholders or cause them any tangible damage.

On 19 November 2013, a new Bank of Israel directive was published on the subject of remuneration policy in a banking corporation (Regulation 301A), and following an update of remuneration policy in accordance with the new directive and the approval of the policy by the Remuneration Committee and the Board of Directors, a Special General Meeting was called which was held, as mentioned, on 11 February 2014.

Remuneration of Senior Office-holders

For the year ended 31 December 2013

Below are details of the benefits and amounts which were paid or provided in the years 2013 and 2012 to the Chairman of the Board of Directors and to the five recipients of the highest salaries among the senior office holders of the Group. The benefits described below do not include benefits in respect of banking services that are granted to all employees, such as benefits regarding interest on deposits of monies with the Bank, interest benefits in respect of mortgages, discounts or exemptions from commissions for banking services provided by the Bank. The amounts of the benefits in respect of the banking services mentioned, regarding each recipient, are not material. Certain private banking customers, including customers who are included in arrangements between the Bank and employee groups, are occasionally awarded benefits that are similar to those granted to Bank employees and in some cases, even exceed them.

2013												
Details of recipient of remuneration (1)			Remuneration for services			Other remuneration			Loans given on beneficial terms (14)			
Name	Position	Holding in the capital of the Bank	Salary	Bonuses (8)	Social benefit provisions (3)	Share-based payment(8)	Value of the benefit (4)	Total (2)	Balance as at 31 December 2013	Average period until maturity (years)	Benefit provided over the year	Loans granted on regular terms
		%	NIS thousands									
Mr. David Brodet (5)	Chairman of the Board of Directors	**0.001**	**2,164**	**962**	**997**	**962**	**156**	**5,241**	**-**	**-**	**-**	**-**
Ms. Rakefet Russak-Aminoach (6)	President and Chief Executive Officer	**0.003**	**2,360**	**1,453**	**1,178**	**1,153**	**141**	**6,285**	**91**	**1.42**	**4**	**25**
Professor Daniel Tsiddon (9)	Deputy Chief Executive Officer, Head of Capital Markets, Private Banking and Strategy Division	**-**	**1,500**	**660**	**439**	**669**	**111**	**3,388**	**81**	**1.42**	**3**	**50**
Mr. Gidon Altman (10)	Formerly, Executive Vice-President, Head of the Commercial Banking Division	**0.001**	**1,353**	**599**	**8,229**	**599**	**118**	**10,898**	**-**	**-**	**-**	**13**
Mr. Yitzhak Eyal (11)	Former General Manager of Bank Leumi (USA)	**0.002**	**1,546**	**849**	**1,386**	**-**	**718**	**4,499**	**94**	**1.21**	**5**	**5**
Mr. Yaron Bloch (12)	General Manager, Leumi Partners	**-**	**1,212**	**2,000**	**314**	**-**	**123**	**3,649**	**-**	**-**	**-**	**-**
Mr. Dan Yerushalmi (13)	Executive Vice-President, Head of Operations and Information Systems Division	**-**	**1,137**	**1,248**	**537**	**702**	**14**	**3,639**	**-**	**-**	**-**	**-**

1. Those receiving remuneration hold full-time positions.

2. Excluding salary tax.

3. Social benefit provisions include provisions for severance pay, provident funds, pension, supplementary training fund, vacations, jubilee bonus, non-competition period, and national insurance, as well as supplemental reserves in respect of the above, due to salary changes during the accounting year.

4. The value of the benefit includes, *inter alia,* a car and telephone expenses.

5. On 4 November 2010, the General Meeting of the Bank approved the terms of engagement between the Bank and the Chairman of the Board of Directors, Mr. David Brodet. The Chairman is employed on a full-time basis as an Executive Chairman. For details of the terms of employment of the Chairman, see Note 15(B)(4) to the Financial Statements. On 11 February 2014, following the approval of the Board of Directors and the Remuneration Committee, the General Meeting approved a resolution that the Chairman of the Board of Directors is entitled to a performance-contingent annual bonus, subject to the provisions of the remuneration policy for office-holders in the Bank for each of the years 2013, 2014, 2015 and 2016. For a summary of the details of the Bonus Plan, see note 15G, to the financial statements.

6. Ms. Rakefet Russak-Aminoach serves as President and Chief Executive Officer of the Bank and the Group from 1 May 2012. For further details regarding the terms of office of the President and Chief Executive Officer, see note 15B(3)(a). The President and CEO, who had a first-generation employee agreement with the Bank, transferred, with effect from 2013, to the employment terms of a second-generation agreement, as follows: the rights of the President and CEO to a non-contributory pension from the Bank pursuant to her rights as first-generation, will be only in respect of the frozen salary level (the salary of the President and CEO at the date of the transfer from first-generation to second-generation plus linkage to the consumer price index) with her rights with regard to the salary increment in excess of the frozen salary level being according to the second-generation conditions (provisions for provident fund without the rights to non-contributory pension from the Bank). On 11 February 2014, following the approval of the Board of Directors and the Remuneration Committee, the General Meeting of the Bank approved an update of the retirement terms of the President and CEO, as follows: (1) in the event of the resignation of the President and CEO from her post in the Bank after completing three years in office as the President and CEO, she will be entitled to remuneration of an amount equivalent to 250% of the last known monthly salary at the time of terminating employee-employer relations between her and the Bank times the number of years of her employment in the Bank, with the addition of provisions for remuneration. (2) It is clarified that "dismissals" with regard to the President and CEO will include both resignation as a result of a deterioration of the terms of employment, including resignation as a result of changes that occur in the Bank and which do not allow the President and CEO to continue to function as a President and CEO, this in the opinion of the President and CEO, with the approval of the Remuneration Committee or the Board of Directors. (3) In the event of dismissal of the President and CEO from her position in the Bank after completing three years of her term of office as President and CEO, she will be entitled to choose between one of the following two alternatives: (a) severance pay in an amount equivalent to 200% of the last known monthly salary at the time of terminating employee-employer relations between her and the Bank times the number of years of her employment in the Bank, with the addition of provisions for remuneration; or (b) an immediate retirement allowance from the Bank according to the first-generation conditions which transferred to second generation. The General Meeting also approved, following the approval of the Board of Directors and the Remuneration Committee, that the President and CEO is entitled to a performance-contingent annual bonus and to a fixed annual bonus in accordance with and subject to the provisions of the office-holders in the Bank's remuneration policy, for each of the years 2013, 2014, 2015 and 2016. For a summary of the details of the Bonus Plan, see note 15G, to the financial statements.

7. Senior employees of the Bank have special personal employment agreements with the Bank. For further details regarding the retirement conditions of senior officers and entitlement to advance notice on terminating employment, see note 15B(3)(c) to the financial statements.

   For the purpose of explanations regarding the senior employees' annual bonus pursuant to the Bank's new bonus plan, see 8. below.

Members of the Bank management who had a first-generation employee agreement in the Bank with effect from 2013 have transferred to the employment terms of a second-generation agreement, as follows: their rights to a non-contributory pension from the Bank pursuant to their rights as first-generation will be only in respect of the frozen salary level (the salary at the date of the transfer from first-generation to the second-generation plus linkage to the consumer price index), with the rights with regard to the salary increments in excess of the frozen salary being according to the second-generation conditions (provisions for provident fund without the rights to a non-contributory pension from the Bank).

The maximum additional expense that the Bank may incur, in the event of the abovementioned employees being immediately dismissed, amounts to NIS 388 million (2012 – NIS 364 million) These amounts are before tax and include salary tax on the pension obligation. Since it is not likely that all the said employees will be dismissed immediately, a global provision of 25% of the above amount has been made, amounting to NIS 97 million (2012 - NIS 110 million). These amounts also relate to members of Management and to the President and CEO. Following the amendment to the personal contracts of the members of management, as set forth in note 15B(3)(c) to the financial statements, a specific attribution out of the said provision was made for members of management, the balance of which amounted to NIS 24 million as of 31 December 2013; in 2012 – NIS 12 million.

8. On 11 February 2014, the General Meeting of the Bank approved the remuneration policy for office-holders in the Bank in respect of the years 2013 – 2016, following the approval of the Board of Directors in accordance with the approval and recommendations of the Remuneration Committee. The remuneration policy is based on the provisions of Amendment 20 to the Companies Law with regard to the term of office and employment of office-holders in the Bank and the provisions of Proper Conduct of Banking Business Management Regulation no. 301A regarding Remuneration Policy in a Banking Corporation. For details, see Note 15G to the Financial Statements.

9. Professor Daniel Tsiddon serves as Head of the Capital Markets, Private Banking and Strategy Division in the Bank. The salary of Professor Tsiddon, as set forth in the table above, is in accordance with the Bank's remuneration policy as regards the remuneration of senior officers in the Bank. Details regarding the retirement terms of senior officers in the Bank and their entitlement to early notice on termination of employment – see note 15B(3)(c) to the financial statements. Professor Tsiddon is entitled to a performance-contingent annual bonus in respect of 2013, as noted in the above table, pursuant to the provisions of the Bank's remuneration policy – see 8. above. One half of the performance-contingent annual grant will be paid to Professor Tsiddon in cash and half of the performance-contingent will be deferred and spread over three years and will be granted by means of performance share units – see note 15G to the financial statements.

10. Mr. Gidon Altman ceased to serve in his position as Head of the Commercial Division on 31 December 2013. The retirement and advance notice conditions to which Mr. Altman is entitled are according to the retirement conditions of the senior officers in the Bank who have a first-generation employment agreement, see note 15B(3)(c) to the financial statements. According to this employment agreement, Mr. Altman is entitled to choose early pension from the date of his retirement and thereafter, at a rate of 70% of his last salary or severance pay. In addition, Mr. Altman is entitled a performance-contingent annual bonus in respect of 2013, as noted in the table above, in accordance with the provisions of the Bank's remuneration policy – see 8. above. One half of the performance-contingent annual bonus will be paid to Mr. Altman in cash and half of the performance-contingent annual bonus will be deferred and spread over three years, and will be granted by means of performance share units – see note 15G to the financial statements.

11. Mr. Yitzhak Eyal ceased to serve in his position in the Bank in December 2013. Mr. Eyal served as general manager of Bank Leumi USA (Leumi USA) , a wholly-owned and controlled subsidiary of the Bank until 31 August 2013. Mr. Eyal's salary in respect of his term of office as general manager of Leumi USA was determined in accordance with customary practice for general managers of banks of a similar size and activity in the United States. Mr. Eyal's salary in respect of his term of office as general manager of Leumi USA also included additional rental expenses for a general manager in the United States. The decision to award Mr. Eyal a bonus as noted in the table above in respect of his term of office as general manager of Leumi USA was approved in the board of directors of Leumi United States. The decision of Leumi USA to award Mr. Eyal a bonus was made further to and in accordance with the remuneration policy of the Leumi Group for general managers in overseas subsidiaries and was passed, *inter alia*, against a background of the operating results achieved by Leumi USA in 2013.

For details regarding the retirement conditions of senior officers in the Bank, including Mr. Eyal and his entitlement to early notice on termination of employment, see note 15B(3)(c) to the financial statements.

12. Mr. Yaron Bloch serves as General Manager of Leumi Partners Ltd ("**Leumi Partners**"), a wholly owned and controlled subsidiary of the Bank, with effect from 1 January 2011. According to the employment agreement between the parties, each party may bring this agreement to an end at any time - in the event that Mr. Bloch resigns from his position, he must give three months' advance notice, and in the case of dismissal, Leumi Partners must give Mr. Bloch 12 months' advance notice. On the termination of Mr. Bloch's employment, due to resignation or dismissal, he will be entitled to all of the monies which have accrued to his credit in the managers insurance policy maintained for him, including the amounts in respect of severance pay. In the event that employment relations are terminated between the parties in circumstances which entitle Mr. Bloch to severance pay according to the law, he will also be entitled to the difference between the severance pay due to him according the law and the amounts accrued on account of severance pay in the managers insurance, insofar as there is a difference. Pursuant to the provisions of the employment agreement, Mr. Bloch is entitled to an annual bonus, which will be calculated according to return on capital in that year, in accordance with the provisions of the employment agreement, providing that the amount of the annual bonus does not exceed the ceiling provided in his employment agreement. In the event of the termination of employment in the middle of a year, for any reason, Mr. Bloch will be entitled to payment of the bonus in respect of the proportional part of the year that he was actually employed, providing that he was actually employed in a period which is not less than six calendar months in that year.

13. Mr. Dan Yerushalmi serves as Head of the Operations and Computers Division in the Bank with effect from 1 March 2013. Mr. Yerushalmi's salary, as set forth in the above table is in accordance with the Bank's remuneration policy as regards senior officers in the Bank. For details regarding the retirement conditions of senior officers in the Bank and their entitlement to early notice on termination of employment, see note 15B(3)(c) to the financial statements. Mr. Yerushalmi is entitled to a performance-contingent annual bonus in respect of his term of office 2013, as noted in the above table, in accordance with the remuneration policy of the Bank – see 8. above. One half of the performance-contingent annual bonus will be paid to Mr. Yerushalmi in cash and half of the performance-contingent annual bonus will be deferred and spread over three years, and will be granted by means of performance share units – see note 15G to the financial statements. In addition, the Board of Directors and the Remuneration Committee decided to award Mr. Yerushalmi, in accordance with the Bank's remuneration policy, an enlistment bonus of ten salary amounts (in respect of half of the commencement of his term of office in the Bank in 2013 and one-half after finishing his first year in office at the Bank at the end of February 2014). One half of the enlistment bonus will be paid in cash and half of the enlistment bonus will be deferred and spread over three years, and will be granted by means of restricted share units.

14. Loans granted under terms generally excepted for all employees in the Bank and their amounts have been determined according to consistent criteria.

15. Directors and other officers have been insured by the Bank under directors' and other officers' liability insurance policies covering the Bank and its investee companies. The proportional insurance premium paid is not included in the above tables, as it is insignificant. The total premium amounted to NIS 3,351 thousand and relates to all officers in the insured group.

16. Having held discussions, received explanations and appropriate and relevant background material, and having examined the remuneration, taking into account the activities of the Bank and the Group and their results in 2013, and after noting the Bank's remuneration policy and the performance and activity of each senior officer, the Board of Directors believes that the payments to abovementioned senior officers, as set out in the table and the explanations above, represent fair and reasonable remuneration under the circumstances.

For further details, see Note 15 to the financial statements.

2012												
Details of party receiving remuneration			Remuneration for services			Other remuneration			Loans given on beneficial terms			
Name	Position	Holding in the capital of the Bank	Salary	Bonuses	Social benefit provisions	Share-based payment	Value of the benefit	Total *	Balance as at 31 December 2013	Average period until maturity (years)	Benefit provided over the year	Loans granted on regular terms
		%	NIS thousands									
Mr. David Brodet	Chairman of the Board of Directors	0.001	2,119	-	1,029	-	154	3,302	-	-	-	-
Ms. Rakefet Russak-Aminoach	President and Chief Executive Officer	0.003	2,063	(353)	3,308	-	140	5,158	88	2.42	3	103
Ms. Galia Maor	(Formerly) President and Chief Executive Officer	0.021	2,891	(727)	(91)	-	133	2,206	180	2.42	11	22
Mr. Baruch Lederman	Executive Vice President, Head of Banking Division	-	1,493	(242)	5,883	-	110	7,244	301	5.98	16	233
Mr. Yehoshua Borstein	General Manager, Leumi Mortgage Bank	-	1,012	161	5,473	-	88	6,734	67	1.81	5	-
Mr. Amnon Zaidenberg	Chief Executive Officer, Bank Leumi (Switzerland)	-	1,919	2,038	733	-	367	5,057	-	-	-	-
Mr. Itzhak Eyal	Chief Executive Officer, Bank Leumi USA	0.002	1,976	1,120	843	-	785	4,724	116	2.14	7	-
Mr.Yitzhak Malach	Head of Operations and Information Systems Division	0.008	1,479	(239)	2,083	-	147	3,470	244	3.41	12	175
Ms. Tamar Yassur **	Vice President Head of Banking Division	-	1,030	1,500	777	-	72	3,379	-	-	-	-
Mr. Zvi Itskovitch	(Formerly) Senior Vice President and Head of International and Private Banking Division	-	1,480	(203)	1,953	-	120	3,350	240	4.07	13	20

* Excluding salary tax.
** The bonus relates to 2011-2012.

Auditors' Fees (1)(2)(3)

	Consolidated		Bank	
	2013	2012	**2013**	2012
	NIS thousands			
For auditing activity: (4)				
Joint auditors	**28,895**	30,742	**14,345**	12,898
Other auditors	**4,058**	4,499	**271**	254
Total	**32,953**	35,241	**14,616**	13,152
For audit related services: (6)				
Joint auditors	**343**	355	**64**	27
Other auditors	**34**	406	**-**	-
For tax services: (5)				
Joint auditors	**1,549**	1,836	**506**	504
Other auditors	**592**	502	**-**	-
For other services:				
Joint auditors	**2,230**	3,860	**1,586**	3,054
Other auditors	**1,493**	474	**1,211**	-
Total	**6,241**	7,433	**3,367**	3,585
Total auditors' fees	**39,194**	42,674	**17,983**	16,737
Joint auditors' fees from other engagements (7)	**-**	-	**-**	-

(1) Report of the Board of Directors to the Annual General Meeting on the auditors' fees in respect of audit and additional services, under sections 165 and 167 of the Companies Law, 1999.

(2) Auditors' fees include payments to partnerships and corporations under their control and also payments required by the VAT Law.

(3) Including fees paid and accumulated fees.

(4) Audit of annual financial statements and review of interim reports.

(5) Services provided related to routine tax auditing.

(6) Audit related fees, mainly include: prospectuses, special certificates, comfort letters, tax consultancy, forms and reports to authorities to which the signature of the auditors is required and audit of businesses purchased during the year.

(7) As reported by the joint auditors, pursuant to section 4 of the directives relating to a conflict of interests and impairment of independence in consequence of the auditors' other engagements, and included above.

Members of the Board of Directors

The Board of Directors number 15 directors. The legal quorum for discussions is the majority of the directors, with a third being external directors.

Pursuant to Proper Conduct of Banking Business Directive No. 301 of the Supervisor of Banks, at least one-third of the members of the Board of Directors shall be external directors who meet the eligibility requirements of an external director as defined in Proper Conduct of Banking Business Regulation 301.

Accordingly, eight directors who are classified as external directors serve on the Board of Directors, three of whom are external directors pursuant to the provisions of the Companies Law, 1999 ("external directors pursuant to the provisions of the Companies Law").

In addition, in light of the definition of an "independent director" in the Companies Law, the Audit Committee of the Board of Directors confirmed that the external directors pursuant to Proper Conduct of Banking Business Directive No. 301 of the Banking Supervision Department and the external directors pursuant to the provisions of the Companies Law are independent directors.

Pursuant to the provisions of the Companies Law and its Regulations, the Board of Directors of the Bank has resolved that, a minimum number of three directors with "accounting and financial expertise", will serve on the Board of Directors of the Bank at all times, so as to allow the Board of Directors to comply with the requirements imposed upon it by law and the documents of incorporation, and in particular with regard to its responsibility for examination of the financial position of the Bank and the preparation of the financial statements.

In determining the said minimum number, the Board of Directors considered the size of the Bank, the complexity of its activities and the range of risks involved therein, and the systems and procedures in place at the Bank, such as control, risk management, compliance, internal audit, and the audit of the external auditors. It was also taken into account that all of the members of the Board of Directors comply with the qualification requirements to serve as a director of the Bank pursuant to the law.

At least three directors who comply with the definition of a "director with accounting and financial expertise" participate in the discussions of the plenum of the Board of Directors regarding the financial statements and their approval.

Most of the directors serving on the Board of Directors comply with the definition of a director with accounting and financial expertise.

With effect from 1 January 2013, and pursuant to Proper Conduct of Banking Business Directive No. 301 of the Supervisor of Banks, the discussions relating to the financial statements are held in the Audit Committee of the Board of Directors. Pursuant to the directives of the Bank of Israel, the Board of Directors has determined that at least three "directors with accounting and financial expertise" will serve on the Audit Committee of the Board of Directors at all times. Most of the directors serving on the Board of Directors comply with the definition of a director with accounting and financial expertise. The legal quorum for discussion and the approval of resolutions in the Audit Committee will be a majority of the members of the committee, providing that a majority of those present are external directors who are also independent, and at least one of them is an external director pursuant to the provisions of the Companies Law. Seven directors currently serve on the Audit Committee, of which five are external directors, including three directors who are external directors pursuant to the provisions of the Companies Law.

Name of Director	Membership in the committees of the Board of Directors, is the director independent / an external director as defined in the Companies Law / Proper Conduct of Banking Business Management no 301?	Education and employment in the past five years, giving details of professions or areas in which education has been acquired, the institution in which the academic degree or professional certificate which he holds was acquired, and details of the corporations in which he acts as director	Does the company regard him as having accounting and financial expertise?
David Brodet	Chairman of the Board of Directors, chairman of the following committees: Credit, Risk Management, Resources Committee, Procedure Committee, Committee for Examining Conflicts of Interests, Investments Committee, Strategy Committee and member of Foreign Customers Committee Is not an external director/independent	Academic education – B.A. in Economics and Political Science and M.A. in Economics, The Hebrew University of Jerusalem. Chairman of the Board of Directors – Bank Leumi Le-Israel B.M. and Bank Leumi United States, owner of David Brodet Ltd. (in suspension), Chairman of the Executive Committee of the Jerusalem Foundation, the Hadassah Academic College. and the Economic Research Institute of Dr. Yeshayahu Forder (R.A.), member of the Managing Committee of the Jerusalem Institute for Israel Studies and of the Cameri Theater. Chairman of the Board of Trustees of the Fund for Treatment of Sheltered Persons. Lecturer at the National Security College (Haifa University) and President of the Union of Banks in Israel (R.A.) Till December 2012, Chairman of the Public Council for Statistics; till August 2011, member of the committee for locating a manager for the Income Tax Authority; till 2010, Chairman of the Executive Committee of Ben-Gurion University, Chairman of the Investment Committee in the Insurance Fund for Employees of the Provident and Pension Fund of the Histadrut and Mivtachim Institute for Social Insurance of Employees Ltd., external director in Alony-Hetz Property and Investments Ltd.; till July 2010, external director in the Israeli Corporation Ltd., chairman of the body of trustees in the Maurice Falk Institute for Economic Research in Israel Ltd., academic manager in the Caserea Forum (Convention) of the Israel Democracy Institute, member of the council of managers in Mishkenot Sha'ananim and member of the Advisory Committee in the Samuel Neeman Institute for Advanced Studies at the Technion Israel Institute of Technology; till June 2010, Chairman of the Advisory Committee for Exemptions and Mergers with the Antitrust Commissioner; till January 2010, lecturer in the Inter-Disciplinary Center, Herzlia (Business Management and Governance) and the College of Law and Business, Ramat Gan; till April 2009, editor of Israel 2028 – Vision and Socio-economic Strategy in a Global World"; till 2009, director in Global Medical Network; till December 2009, member of the committee in charge in the Blue Square Cooperative Association Ltd.	YES. Chairman of the Board of Directors of the Bank since August 2010. B.A. in Economics and Political Science and M.A. in Economics, Hebrew University, Jerusalem VP Finance of Israel Aircraft Industries 1987-1991 Budgets Director in the Ministry of Finance 1991-1994 Director-General, Ministry of Finance 1995-1997 Served as Chairman of the Board of Directors of Mizrahi Bank and Tefahot Bank, and as Chairman of Karnit Government Insurance Corporation. Served as Director of Public Companies and as a Member of Finance and Financial Statements Committees of various Boards of Directors.

Name of Director	Membership in the committees of the Board of Directors, is the director independent / an external director as defined in the Companies Law / Proper Conduct of Banking Business Management no. 301?	Education and employment in the past five years, giving details of professions or areas in which education has been acquired, the institution in which the academic degree or professional certificate which he holds was acquired, and details of the corporations in which he acts as director	Does the company regard him as having accounting and financial expertise?
David Avner	Member of Credit Committee, Resources Committee, Committee for Examining Conflicts of Interests, Strategy and Committee for Examining a Claim (*ad hoc*) Is not an external director / independent	Academic education - B.A. in Mathematics, Computer Sciences and Philosophy, Haifa University, and M.B.A, Haifa Technion Chief Executive Officer and Owner of N.S.Y. Avner Ltd. Member of the Executive Committee in the Technion – Israel Institute of Technology Lecturer in the Association of Kiryat Academit Kiryat Ono College in the Business Administration Faculty CEO of Partner Communications Ltd. – till 2010.	YES B.A. in Mathematics and Philosophy, Haifa University, and M.B.A, Haifa Technion, CEO and Deputy CFO in Partner Communication Ltd., a public company traded on the Tel Aviv Stock Exchange, 2005-2010. As part of his function as CEO of the company, he was heavily involved in the process of preparing financial statements
Rami Avraham Guzman	External director, member of Credit Committee, Prospectuses Committee, Procedure Committee and Strategy Committee Independent/external director pursuant to Proper Conduct of Banking Business Management Regulation 301	Academic education - M.B.A in Business Administration and Public Administration and B.A. in Economics and Political Science, The Hebrew University of Jerusalem. Member of Research Team, Computer Systems Management, Stanford University and Stanford Research Institute. Doctorate studies – Hebrew University, Jerusalem. Chairman of the Executive Committee, from 1993, President of the Association of Beit Zvi – School for Performing Arts, director in the academic stream of the College for Management founded by the Tel Aviv Clerks Organization Public Benefit Company Ltd., and Ampa Capital Ltd., Tower Semiconductor Ltd., and Gmul Investment Company, owner and general manager and director of Rami Guzman Initiation and Advice, Member of Investment Committee, Israel Infrastructure Fund 1-A, L.P., Israel Infrastructure Fund 1-B, L.P. and Israel Infrastructure Fund 1-C, L.P. Member of Exposure Committee, B.S.S.CH., – The Israeli Credit Insurance Company Ltd., member of the Executive Committee in the Israel-America Bureau and Member of the Executive Committee Chairman of the Executive Committee of the Zeev Gorodetsky Scholarship Fund. Till 2012, director in Epcon Electro Mechanics Ltd. (Epcon Technologies Ltd.) in Africa-Israel Investments Ltd. and member in the Appeals Committee to the Encouragement of Investments Law. Till 2011, director in Bank Leumi Le'Israel Ltd, in Adamind Ltd and in Micromedic Technologies Ltd.	YES B.A. in Economics and Politics and M.B.A in Public Administration, The Hebrew University of Jerusalem. Member of Research Team, Computer Systems Management, Stanford University and Stanford Research Institute. Various economic and technological positions in the Ministry of Finance, 1962-1969, 1971-1977 CFO in Electrochemical Industries and Frutarom, 1977-1982. CFO of Elscint 1982-1983, CEO of Dikla Holdings, 1983-1985, CFO in Motorola Communications and Motorola Israel, 1985-2004, Vice-President Motorola Inc., 2001-2005, Director in Bank Leumi, 2005-2011.

Name of Director	Membership in the committees of the Board of Directors, is the director independent / an external director as defined in the Companies Law / Proper Conduct of Banking Business Management no. 301?	Education and employment in the past five years, giving details of professions or areas in which education has been acquired, the institution in which the academic degree or professional certificate which he holds was acquired, and details of the corporations in which he acts as director	Does the company regard him as having accounting and financial expertise?
Prof. Arieh Gans	External director, member of Credit Committee, Audit Committee, Prospectuses Committee and Committee for Examining Conflicts of Interests Independent/external director pursuant to Proper Conduct of Banking Business Management Regulation no. 301	Academic education – C.P.A. (Isr.), B.A. in Accounting, The Hebrew University of Jerusalem (Tel Aviv Branch) Professor of Accounting, Tel Aviv University and Company Director. Member of Professional Committee in the Israeli Accounting Standards Board. Till 2013, member of Finance and Audit Committee, Middle East Tube Company Ltd. Till 2010, owner, director and general manager of A. Gans Management and Consultancy Services Ltd.	YES C.P.A. (Isr.), B.A. in Accounting, The Hebrew University of Jerusalem (Tel Aviv Branch), Professor of Accounting, Tel Aviv University. Held various accounting positions with Koor Industries Ltd., 1978-1998, including Vice President Accounting and Control and Head of Accounting Division. Kesselman & Kesselman, Certified Public Accountants (Isr.), 1961-1977. Member of various committees of the Israeli Institute of Certified Public Accountants, the Israeli Accounting Standards Board and Senior Examiner of the Auditors' Council. Director of various companies.
Moshe Dovrat	Member of Risk Management Committee, Resources Committee, Prospectuses Committee Procedures Committee and Investments Committee Not an independent/external director	Academic education - B.A. in Economics and Political Science and M.B.A., The Hebrew University of Jerusalem CEO, Director and Owner of Dovrat (M.H.) Investments and Business Initiatives Ltd. and Beit Meniv Funding Ltd Shareholder and director in Beit Meniv Israel Ltd. and Theracoat Ltd. Member of Executive Committee of the Ra'anana Symphonette Orchestra, Member of the General Assembly and one of the founders of the Macro Center for Political Economics and Sustainable Eco-Tourism in Israel, Member of the Public Council of the Batsheva Dance Company. Member of the Finance Committee for the Council for a Beautiful Israel. Member of the General Assembly of the Ramat Gan College and the Academic Israel College in Ramat Gan, Member of Management of Kfar Blum Holdings – Agricultural Cooperative Society (Pastoral Hotel), Member of the Israel - Czech Republic Chamber of Commerce – and director in the Review of Members of the Institute of Certified Public Accountants in Israel Ltd. and in Kfar Blum Kayaks and Bet Hillel; till 2012, director in The Jewish-Arab Center for Economic Development.	YES B.A. in Economics and Political Science and M.B.A., The Hebrew University of Jerusalem Held various economic positions with the Bank of Israel and Ministry of Finance, 1968-1975; Vice President of an industrial company, 1975-1980; Head of Foreign Currency Investments and Deposits Department of Bank Hapoalim, 1980-1985; held various positions as an economist with the Ministry of Economics and Planning, including Director-General of the Ministry, 1985-1989; Head of Economic Department of Clalit Health Services, 1989-1992; Head of the Investment Center of the Ministry of Industry, Trade and Labor, 1992-1996. Chairman of the Board of Directors, director and member of investment committees, and CEO of various companies.

Name of Director	Membership in the committees of the Board of Directors, is the director independent / an external director as defined in the Companies Law / Proper Conduct of Banking Business Management no. 301?	Education and employment in the past five years, giving details of professions or areas in which education has been acquired, the institution in which the academic degree or professional certificate which he holds was acquired, and details of the corporations in which he acts as director	Does the company regard him as having accounting and financial expertise?
Shay Shachnai Hermesh	Member of Risk Management Committee, Procedure Committee, Investments Committee and Strategy Committee Not an independent/external director	Academic education – B.A. in Business Administration at the Hebrew University, Jerusalem, specializing in employment relations and finance, Hebrew University, Jerusalem. Chairman of the Israeli Management, World Deputy President and member of the Steering Committee in the World Jewish Congress and director in Kafrit Industries (Public corporation). Till 2013, director in Sapir College of Education and member of the Knesset.	YES – Treasurer in Kibbutz Kfar Aza, Head of Sha'ar Hanegev Regional Council. (including treatment with banks according to the Kibbutz Arrangement), Chairman of the Sha'ar Hanegev Regional Plants Finance Committee, Chief Financial Officer of Kafrit Industries (Public corporation), Treasurer of the Jewish Agency and Zionist Histadrut, member of Knesset Finance Committee (2006-2013), member of the Financial Statements Committee (formerly) – "Frutarom", Kafrit, Chairman of the Executive Committee, Sapir College and Head of the Investment Committee, Academic background in the field: B.A. in Economics and Business Administration. specializing in employment relations and finance, Hebrew University, Jerusalem
Adv. Miriyam (Miri) Katz	Chairman of the Prospectuses Committee and member of Audit Committee, Procedure Committee and Strategy Committee Not an independent/external director	Academic education – Graduate in Law, Hebrew University, Jerusalem Director in Itamar Medical Ltd. CEO, Ima fund, (R.A.). (philanthropic fund) Member of the Board of Trustees of the Hebrew University in Jerusalem, and the Technion Israel Institute of Technology Till 2010, Director in Edmond and Nadine de Rothschild Find Israel (philanthropic fund). Till 2009, director in Edmund Binyamin de Rothschild Development Company Ltd. and Edmond de Rothschild Caesarea Fund.	YES - LL.B, The Hebrew University of Jerusalem Chairperson of the Israel Securities Authority, 1997-2002 Member of the Auditors' Council, 1997-2002 External Director and Chairperson of the Audit Committee, Bank of Jerusalem, 2003-2006 Managing Partner, Ophir Katz & Co., Law Offices 1989-1997; Advisor since 2003 External Director and director of various companies
Yoav Nardi	Member of Credit Committee, Audit Committee, Committee for Examining Conflicts of Interests, Foreign Customers Committee and Committee for Examining a Claim (*ad hoc*) Not an independent / external director	Academic education - B.A. in Economics and M.B.A. (Finance), The Hebrew University in Jerusalem. Chairman of Investments Committee of the National Library Ltd. and Yad Sarah (R.A.) Director and Owner of Nardi Consultants and Risk Management Ltd. Till 2010, Jerusalem Bank, advisor to the General Manager, assistant to the General Manager, and member of management, Head of Risk and Nostro Section and Financial Risk Manager. Director in Jerusalem Capital Markets Funds (1980) Ltd. Ir Shalem Insurance Agency (1996) Ltd. and Jerusalem Bank Trust Company Ltd, and Chairman of the board of directors in Jerusalem Finance and Issues (2005) Ltd. and Jerusalem Financial Operation (2005) Ltd.	YES - B.A. in Economics and M.B.A. (Finance), The Hebrew University in Jerusalem. Has wealth of diverse banking experience in the fields of credit, financial markets and asset and liability management. Served in a wide range of positions in the Banking Supervision Department of the Bank of Israel, and as a Chief Economist at the First International Bank. Served as member of Management and Deputy President and Chief Executive Officer of the Jerusalem Bank and was involved on an ongoing basis in monitoring the preparing the Financial Statements of Bank Jerusalem, including the Directors Report.

Name of Director	Membership in the committees of the Board of Directors, is the director independent / an external director as defined in the Companies Law / Proper Conduct of Banking Business Management no. 301?	Education and employment in the past five years, giving details of professions or areas in which education has been acquired, the institution in which the academic degree or professional certificate which he holds was acquired, and details of the corporations in which he acts as director	Does the company regard him as having accounting and financial expertise?
Haim Samet	Director from the public, Remuneration Committee, member of the Audit Committee, Resources Committee, Prospectuses Committee, Investment Committee and Committee for Examining a Claim (*ad hoc*). Independent / external director as defined in the Companies Law and Proper Conduct of Banking Business Management Regulation no. 301	Academic education – .A. in Law, The Hebrew University in Jerusalem, Tel Aviv branch Joint Senior Partner in law firm: Schnitzer, Gottlieb Samet & Co., Director and Deputy Chairman in Tel Aviv Museum of the Arts Ltd., Director in Tekoa Mushroom Farm Ltd. H.Y.D. Properties Ltd., Keren Ya'ar Investments Ltd., in H.Y.D.A. Holdings Ltd. in H. Samet Attorneys. From 2011, Member of Board of Trustees and Chairman of the Audit Committee in Tel Aviv University Till 2009, partner in Haim Samet, Steinmetz, Haring & Co, Attorneys. Till December 2013, director in H.Y.D. Trustees (1991) Ltd. in H.Y.D. Services (1991) Ltd.	YES - B.A. in Law, The Hebrew University in Jerusalem. Director in Bank Leumi. Served as member of the Credit and Audit Committee of the Bank, 1995-2000. Director in Bank Hapoalim, where he served as a member of various committees, including its credit committee, audit committee, businesses and budget committee, review of expenditure and streamlining committee and remuneration committee, 2000-2008.
Nurit Segal	Member of Risk Management Committee, Prospectuses Committee, Committee to Examine Conflicts of Interests, Investment Committee Not an independent/external director	Academic education – B.A. in Economics and Statistics – Hebrew University in Jerusalem M.Sc. in Performance Investigation in Case Western Reserve University, Cleveland, Ohio, United States. Director in Aspen Group Ltd. and member of management and chairman of finance committee in Helicon – Song Promotion Union in Israel. Till 2012, director in Olympia – Real Estate Holdings Ltd. Till 2011, director in King Ltd. Till 2010, director in Bank Leumi Le'Israel Ltd. Till 2009, director in Aspen Real Estate Ltd.	YES - B.A. in Economics and Statistics – Hebrew University, Jerusalem Term of office in the boards of public companies including the balance sheet committees and chairman of the balance sheet committee. Monitoring developments in financial reporting by means of seminars of accounting firms and email updates
Zipporah Samet	Director from the public, Audit Committee, and member of the Credit Committee, Risk Management Committee, Remuneration Committee, Resources Committee and Committee for Examining Conflicts of Interests Independent / external director as defined in the Companies Law and Proper Conduct of Banking Business Management Regulation no. 301	Academic education – B.A. in Economics and Mathematics and MBA (Economics), Hebrew University in Jerusalem. Owner, Chairman of the Board of Directors and CEO in Merav Yaniv Financial Consulting Ltd. since 2003, External Director in Shahar Hadash Group Ltd. in Africa Israel Investments Ltd. Director and shareholder in Bio-Plasmar Ltd. Till 2012, chairman of the board of directors of Capital Israeli Company for the Location of Money Ltd. Till 2011, external director in Ophir Optronics Ltd. To 2010, external director in Menora Mivtachim Gemel Ltd., in Menora Mivtachim Pension Ltd. and chairman of investments committee in Avner Ltd. Till 2009, external director in Israel Discount Bank Ltd.	YES - B.A. in Economics and Mathematics and MBA (Economics), Hebrew University in Jerusalem. Senior Economist in the Bank Research Unit in the Bank of Israel, Head of Pricing Monitoring and Control Team, 1983-1995. Senior Deputy to the Supervisor of Capital Markets, Insurance and Saving in the Finance Ministry, 1995-1998. Supervisor of Capital Markets, Insurance and Saving in the Finance Ministry, 1998-2002.External Director in Israel Discount Bank Ltd., including term as Chairman of the Audit Committee, 2003-2009.

Name of Director	Membership in the committees of the Board of Directors, is the director independent / an external director as defined in the Companies Law / Proper Conduct of Banking Business Management no. 301?	Education and employment in the past five years, giving details of professions or areas in which education has been acquired, the institution in which the academic degree or professional certificate which he holds was acquired, and details of the corporations in which he acts as director	Does the company regard him as having accounting and financial expertise?
Amos Sapir	External director, Member of the Audit Committee, Risk Management Committee, Committee for Examining Conflicts of Interests, Strategy Committee and Committee for Examining a Claim (*ad hoc*) Independent / external director as defined in the Companies Law and Proper Conduct of Banking Business Management Regulation no. 301	Academic education – B.A. in Economics and International Relations, Hebrew University in Jerusalem. MBA specializing in Finance, University of Columbia, New York. Doctorate studies, specializing in Finance and Banking – University of Colombia, New York, USA (without degree) External Director in Hot Communication Systems Ltd, and A. Dori Group Ltd, Director in Log Plastic Products (1993) Ltd. and Mifal HaPayis Pinhas Sapir Fund, Director and owner in Sixace Management Co. Ltd (1997) Ltd., and Sixace Holdings Ltd. Member of Board of Trustees in Tel Aviv University and, Member of the Executive Committee in the Academic College of Tel-Aviv-Yafo, and in the Shoshana and Pinhas Sapir Fund Member of the Council in the Educational Technology Center Chairman of the Board of Trustees in the Pinhas Sapir Development Center, Chairman of the Executive Committee in Leadership Jump-Start and Excellence in Employment for Ethiopian Academics, Member on Public Council – Midot – Reflection and Rating of Non-Profit Associations Ltd. (Halatz), Member of Council in Educational Technology Center. Chairman of Board of Trustees in Pinhas Sapir Development Center and member of Association body in Pinhas Sapir Economic Policy Forum, founded by Sam Rothberg. Till 2013, chairman of the board of directors of N. Feldman & Son Ltd. Till 2012, chairman of the board of directors of Ishal Amlet Investments (1993) Ltd. and member of the Board of Trustees of Bezalel Art and Design Academy, Jerusalem. Till 2011, director in Capital Studios Jerusalem Group Ltd. Till 2009, chairman of the board of directors in Standard & Poor's Ma'alot Ltd. Till 2014, director in Israel Management 1 Infrastructures Ltd. and Israel Management 2 Infrastructures Ltd.	YES B.A. in Social Sciences (Economics and International Relations), Hebrew University in Jerusalem. MBA (specializing in Finance) and Doctoral Studies (specializing in Banking Finance), University of Columbia, New York. Economist and manager of investment company, Industrial Development Bank in Israel Ltd, 1967-1968. Economist, Clal (Israel) Ltd., 1968-1969. General Manager – Member of group of founders and shareholder in technology company, Tadah Technological Development and Automation Ltd., 1969-1973. Assistant to the CEO – responsible for the team setting up a new investment company under the ownership of European investors, Industrial Development in Israel Company Ltd., 1974-1975. Deputy Chairman of the Board of Directors and shareholder representative, Israeli Food Produce Ltd., 1975-1978. CEO – in charge of establishment of television plant, Talanit Ltd., 1978-1979. Finance Officer, VP Finance and Administration, Assistant to the CEO and CEO of Clal Real Estate Investments Ltd., Assistant to the CEO, Head of Staff, Chairman of the Board of Directors of A.B.N. Health and Leisure Sites Ltd. (Tourist Division of Clal Group). From January 1996, CEO of Clal Capital Markets and in charge of the Group's capital market activity, Member of many directorial boards of companies in the Clal Israel Ltd., Clal (Israel) Ltd. April 1980-May 1997 Chairman of the Board of Directors, Ma'alot, The Israel Securities Rating Company Ltd. November 1999-January 2008. Chairman of the Board of Directors, Standard and Poor's Ma'alot Ltd. January 2008-October 2009. Chairman of the Board of Directors, N. Feldman & Son Ltd. January 2003-to 31 March 2003. Director (Chairman of the Board of Directors from January 2011), Ishal Malta Investment (1993) Ltd. December 2001-to 29 August 2012. External Director, Hot Communication Systems Ltd, June 2007-to date External Director, Log Plastic Products Ltd, November 2007-to date. External Director, A. Dori Group Ltd., December 2010-to date.

Name of Director	Membership in the committees of the Board of Directors, is the director independent / an external director as defined in the Companies Law / Proper Conduct of Banking Business Management no. 301?	Education and employment in the past five years, giving details of professions or areas in which education has been acquired, the institution in which the academic degree or professional certificate which he holds was acquired, and details of the corporations in which he acts as director	Does the company regard him as having accounting and financial expertise?
Prof. Efraim Sadka	External director, Member of the Remuneration Committee, Risk Management Committee, Resources Committee, Investments Committee, and Foreign Customers Committee. Independent / external director as defined in the Companies Law and Proper Conduct of Banking Business Management Regulation no. 301	Academic education - Ph.D. in Economics, Massachusetts Institute of Technology. B.A. in Economics and Statistics, Tel Aviv University. Professor of Economics, Tel Aviv University Professor of Economics and Holder of the Henry Kaufman Chair of International Capital Markets, Tel Aviv University. Chairman of the Babylonian Jewry Heritage Center. Chairman of the Advisory Committee of Poalim Real Estate Fund External Director of Paz Oil Co. Ltd. Chairman of the Executive Board, The Pinhas Sapir Center for Development, Tel Aviv University. ,Member of the Executive Board of the Sapir Forum, Member of the Association and Chairman of the Audit Committee of the Israel Democracy Institute, Deputy Editor of international professional periodicals, member of the Professional Committee of the Israel Accounting Standards Board. Director in Atidim Ltd. and Rabad Ltd., Owner and Director of A.Z. Eretz Ratz Ltd. Till 2012, chairman of the Bora salary committee (Committee of Heads of Higher Educational Institutions Committees)and director in B. Gaon Holdings Ltd. Till 2011, member of management of Association for Encouragement of Research into Literature and Arts – Achi – Foundation of Iraqi Immigrants to Israel and member of Committee for Examining the Raising of the Retirement Age for Women. Till 2010, member of the Public Committee for Re-examination of the Formula Used in the Allocation of Balancing Grants. Till 2009, Visiting Professor in the Academic Stream of the College of Administration.	YES - .B.A. in Economics and Statistics, Tel Aviv University. Ph.D. in Economics, Massachusetts Institute of Technology. Professor of Economics, Tel Aviv. Member of various professional and public committees, Committee for Examination of a Corporate Governance Code (the Goshen Committee), the Rabinowitz Committee for Income Tax Reform, the Fogel Committee for Pension Reform and the Steinberg Committee for Direct Tax Reform in the Presence of Inflation. Member of the Professional Board of the Israeli Accounting Standards Board. Chairman of the Board of Directors of Housing and Construction Holdings Ltd., 1989-2005. Chairman of the Board of Directors of K.G.M. Pension Fund, 1996-2000. Previously, member and chairman of various boards of directors.

Name of Director	Membership in the committees of the Board of Directors, is the director independent / an external director as defined in the Companies Law / Proper Conduct of Banking Business Management no. 301?	Education and employment in the past five years, giving details of professions or areas in which education has been acquired, the institution in which the academic degree or professional certificate which he holds was acquired, and details of the corporations in which he acts as director	Does the company regard him as having accounting and financial expertise?
Prof. Yedidya Stern	External director, Chairman of the Committee for Examining a Claim (*ad hoc*), member of the Audit Committee, Prospectuses Committee, Procedure Committee, and Investments Committee Independent / external director as defined in Proper Conduct of Banking Business Management Regulation no. 301.	Academic education – .B.A. in Law, Bar Ilan University, M.A. in Law, Harvard University, United States. Professor of Law in Bar-Ilan University, Deputy President for Research in Israeli Democracy Institute .and member and founder of "Tekana Forum" for the Prevention of Sexual Harassment in the Religious Public. Till 2009, director in the Company for the Recovery of Property of Holocaust Victims and a member of the State Investigation to Examine the State's Treatment of Evacuees from Gush Katif and the northern Samaria. Till 2011, External lecturer in Kiryat Academit Ono, Visiting Professor in University of Monash and Chairman of the Professional Committee for Civics Studies in the State of Israel in the Ministry of Education. Till 2012, Member of the Public Committee for the Equality in the Burden.	NO
Prof. Gabriella Shalev	External director, Chairman of the Foreign Customers Committee and member of the Audit Committee, Remuneration Committee, Resources Committee, Procedure Committee, and Strategy Committee Independent / external director as defined in the Companies Law and Proper Conduct of Banking Business Management Regulation no. 301.	Academic education – B.A. in Law, The Hebrew University of Jerusalem, M.A. in Law, The Hebrew University of Jerusalem, Doctor of Law, The Hebrew University of Jerusalem Post-doctoral training in Law- Harvard University, USA . President of the Senior Academic Council and Senior Lecturer in the Ono Academic College. Shareholder in Din Publishing, Management and Services Ltd. Israeli Ambassador at the United Nations in the Foreign Ministry till 2010.	YES - B.A. in Law, The Hebrew University of Jerusalem, M.A. in Law, The Hebrew University of Jerusalem, Doctor of Law, The Hebrew University of Jerusalem. Served for lengthy periods on Boards of Directors of public companies and banks. In some of these companies, served as external director. Served as Director and Head of Audit Committee in Bank Hapoalim.

Board of Directors

During 2013 and until the publication of the Report, the following changes took place in the composition of the Board of Directors:

On 21 March 2013, Mr. Doron Cohen completed his term of office as director in the Bank. Also, on 31 August 2013, Mr. Yehuda Drori completed his term of office as director in the Bank. The Board of Directors expressed its appreciation to Mr. Cohen and Mr. Drori for their contribution to the Bank's business and development. For further details, see the Bank's Immediate Reports dated 21 March 2013 (ref.: 2013-01-013426) and 29 August 2013 (ref.: 2013-01-130731).

On 23 October 2013, the Annual General Meeting of the Bank ("Annual General Meeting") was held, the agenda including. *inter alia*, three items in connection with the directors serving in the Bank: (1) the election of five directors to serve on the Board of Directors, (2) the election of one external director, pursuant to the Companies Law, with effect from 1 February 2014 and (3) the ratification of the term office of an external director, pursuant to the Companies Law – Mr. Haim Samet.

In accordance with the Bank's articles, at the Annual General Meeting, three directors, Mr. David Brodet, Mr. Moshe Dovrat and Mr. Yoav Nardi, retired by rotation.

At the Annual General Meeting, the incumbent directors, Mr. Brodet and Mr. Nardi, were re-elected, and Ms. Etty Langerman, Ms. Nurit Segal and Mr. Shay Hermesh were elected to serve as directors in the Bank. In addition, Professor Gabriela Shalev was re-elected to serve as external director pursuant to the Companies Law, 1999, for a further three-year period commencing 1 February 2014.

On 27 October 2013, notice was received from the Supervisor of Banks of the fact that it was not possible to appoint Ms. Langerman as a director of the Bank, due to an interest of a relative of hers in the Bank (Ms. Langerman's sister is an employee of the Bank). Accordingly, on 28 October 2013, the Bank announced that, pursuant to the provisions of paragraph 2.1.5 of the Bank's Immediate Report concerning the convening of a general meeting dated 16 September 2013 (ref.: 2013-01-147072), Mr. Moshe Dovrat will be considered to have been elected as a director, in place of Ms. Langerman.

Furthermore, it was resolved at the Annual Meeting to ratify the appointment of Mr. Haim Samet as external director pursuant to the Companies Law, 1999.

On 24 October 2013, the Board of Directors approved the term of office of Mr. David Brodet as Chairman of the Board of Directors to the date of completing the procedure for electing the Chairman of the Board of Directors. On 9 January 2014, following receipt of approval from the Bank of Israel on 5 January 2014, the Board of Directors of the Bank approved the term of office of Mr. David Brodet as Chairman of the Board of Directors, till the date of the next general meeting at which the Chairman of the Board of Directors will be nominated for election as a director.

The Banking Supervision Department confirmed the absence of any objection to the terms of office of the directors elected at the said Annual General Meeting.

For further details, see the Bank's Immediate Report pertaining to the results of the Annual General Meeting of 23 October 2013 (ref.: 2013-01-173919) and Immediate Reports dated 24 October 2013 (ref.: 2013-01-174873), 28 October 2013 (ref.: 2013-01-176181, 2013-01-176196) and 12 January 2014 (ref.: 2014-01-011455).

During 2013, the Board of Directors held 45 plenary meetings and 131 committee meetings.

At the Meeting of the Board of Directors that took place on 30 March 2014, it was decided to approve and publish the audited consolidated financial statements of the Group as at 31 December 2013 and for the period ended on that date.

The Board of Directors of the Bank expresses its appreciation and gratitude to the employees and managers of the Bank and Group companies in Israel and abroad for their dedicated work and their contribution to the promotion of the business of the Group.

David Brodet
Chairman of the Board of Directors

Rakefet Russak-Aminoach
President and Chief Executive Officer

30 March 2014

Below are tables of detailed financial information by subjects, segments and periods:

Bank Leumi le-Israel B.M. and its Consolidated Companies
Consolidated Balance Sheet as at end of years 2009-2013

Exhibit A

	2013	2012	2011	2010	2009
	(NIS millions)				
Assets					
Cash and deposits with banks	**44,351**	54,621	53,044	30,052	42,933
Securities	**63,735**	56,408	47,936	55,791	57,505
Securities borrowed or purchased under agreements to resell	**1,360**	1,435	1,225	1,190	744
Credit to the public	**244,757**	245,378	245,287	234,255	215,067
Allowance for credit losses	**(3,883)**	(4,114)	(3,967)	(10,274)	(10,398)
Credit to the public, net	**240,874**	241,264	241,320	223,981	204,669
Credit to governments	**558**	442	448	379	407
Investments in companies included on equity basis	**1,689**	2,129	2,270	1,924	2,178
Buildings and equipment	**3,638**	3,705	3,653	3,638	3,553
Intangible assets and goodwill	**99**	189	181	45	125
Assets in respect of derivative instruments	**13,054**	11,438	11,573	8,717	6,440
Other assets	**5,002**	4,529	4,204	2,605	3,356
Total assets	**374,360**	376,160	365,854	328,322	321,910
Liabilities and equity					
Deposits of the public	**286,003**	289,538	279,404	249,584	250,418
Deposits from banks	**4,310**	4,073	5,056	2,691	3,785
Deposits from governments	**397**	451	519	660	712
Securities lent or sold under agreements to repurchase	**624**	1,007	442	1,006	273
Debentures, bonds and subordinated notes	**25,441**	27,525	29,999	26,939	25,261
Liabilities in respect of derivative instruments	**13,487**	12,762	12,069	9,985	7,559
Other liabilities	**17,333**	15,576	14,737	13,846	12,088
Total liabilities	**347,595**	350,932	342,226	304,711	300,096
Non-controlling interests	**340**	307	254	318	282
Equity attributable to shareholders of the banking corporation	**26,425**	24,921	23,374	23,293	21,532
Total equity	**26,765**	25,228	23,628	23,611	21,814
Total liabilities and equity	**374,360**	376,160	365,854	328,322	321,910

Bank Leumi le-Israel B.M. and its Consolidated Companies
Consolidated Statement of Profit and Loss for the years 2009-2013

Exhibit B

	2013	2012	2011 (1)	2010 (1)	2009 (1)
	(NIS millions)				
Interest income	**12,134**	13,507	14,283	12,489	11,788
Interest expenses	**4,777**	6,099	7,176	5,517	5,277
Net interest income	**7,357**	7,408	7,107	6,972	6,511
Expenses in respect of credit losses	**268**	1,236	734	584	1,521
Net interest income after expenses in respect of credit losses	**7,089**	6,172	6,373	6,388	4,990
Non-interest income					
Non-interest financing income	**1,127**	444	11	475	867
Commissions	**4,188**	4,199	4,116	4,129	3,890
Other income	**202**	131	48	163	350
Total non-interest income	**5,517**	4,774	4,175	4,767	5,107
Operating and other expenses					
Salaries and related expenses	**5,174**	5,290	5,061	4,686	3,896
Building and equipment maintenance and depreciation	**1,833**	1,819	1,704	1,591	1,514
Amortization of intangible assets	**88**	23	2	80	21
Other expenses	**1,838**	1,968	1,574	1,604	1,350
Total operating and other expenses	**8,933**	9,100	8,341	7,961	6,781
Profit before taxes	**3,673**	1,846	2,207	3,194	3,316
Provision for taxes on profit	**1,391**	811	418	1,241	1,272
Profit after taxes	**2,282**	1,035	1,789	1,953	2,044
Banking corporation's share in profits (losses) of companies included on equity basis after tax	**(293)**	(67)	148	420	81
Net profit:					
Before attributing to non-controlling interests	**1,989**	968	1,937	2,373	2,125
Attributed to non-controlling interests	**(42)**	(37)	(46)	(39)	(36)
Attributed to shareholders of the banking corporation	**1,947**	931	1,891	2,334	2,089
Basic and diluted earnings per share:					
Net profit attributed to shareholders of the banking corporation (in NIS)	**1.32**	0.63	1.28	1.58	1.42

(1) Reclassified.

Bank Leumi le-Israel B.M. and its Consolidated Companies
Rates of income and expenses[1] and analysis of changes in interest income and expenses

Exhibit C

Part A – Average balances and interest rates - assets

	2013			2012			2011		
	Average balance[2]	Interest income	Rate of income	Average balance[2]	Interest income	Rate of income	Average balance[2]	Interest income	Rate of income
	(NIS millions)		%	(NIS millions)		%	(NIS millions)		%
Income-bearing assets									
Credit to the public[3,]									
In Israel	209,795	9,700	4.62	209,824	10,460	4.99	200,352	11,166	5.57
Outside Israel	25,799	978	3.79	27,507	1,118	4.06	24,606	971	3.95
Total	235,594	10,678	4.53	237,331	11,578	4.88	224,958	12,137	5.40
Credit to the government									
In Israel	453	23	5.08	412	21	5.10	364	21	5.77
Outside Israel	24	-	-	8	-	-	12	-	-
Total	477	23	4.82	420	21	5.00	376	21	5.59
Deposits in banks									
In Israel	7,480	62	0.83	6,659	76	1.14	7,501	96	1.28
Outside Israel	2,403	13	0.54	3,019	19	0.63	1,610	112	6.96
Total	9,883	75	0.76	9,678	95	0.98	9,111	208	2.28
Deposits in central banks									
In Israel	21,638	309	1.43	21,767	513	2.36	22,303	660	2.96
Outside Israel	4,343	7	0.16	4,387	2	0.05	2,099	3	0.14
Total	25,981	316	1.22	26,154	515	1.97	24,402	663	2.72
Securities borrowed or purchased under resale agreements									
In Israel	1,362	20	1.47	1,819	45	2.47	1,611	47	2.92
Outside Israel	-	-	-	-	-	-	-	-	-
Total	1,362	20	1.47	1,819	45	2.47	1,611	47	2.92
Bonds available for sale [4,5]									
In Israel	41,258	771	1.87	35,736	884	2.47	28,934	881	3.04
Outside Israel	3,940	43	1.09	4,199	82	1.95	4,620	86	1.86
Total	45,198	814	1.80	39,935	966	2.42	33,554	967	2.88
Bonds for trading[4,5]									
In Israel	9,745	206	2.11	10,276	266	2.59	8,526	236	2.77
Outside Israel	314	2	0.64	315	21	6.67	91	4	4.40
Total	10,059	208	2.07	10,591	287	2.71	8,617	240	2.79
Total interest-bearing assets	328,554	12,134	3.69	325,928	13,507	4.14	302,629	14,283	4.72
Receivables for non-interest bearing credit cards	7,037			6,388			6,472		
Other non-interest bearing assets[6]	30,818			30,599			26,575		
Total assets	366,409	12,134		362,915	13,507		335,676	14,283	
Total income-bearing assets attributable to activity outside Israel	36,823	1,043	2.83	39,435	1,242	3.15	33,038	1,176	3.56

See notes on page 275 below.

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

Rates of income and expenses[1] and analysis of changes in interest income and expenses (cont'd)

Exhibit C (cont'd)

Part B – Average balances and interest rates – liabilities and equity

	2013			2012			2011		
	Average balance[2]	**Interest expenses**	**Rate of expenses**	Average balance[2]	Interest expenses	Rate of expenses	Average balance[2]	Interest expenses	Rate of expenses
	(NIS millions)		%	(NIS millions)		%	(NIS millions)		%
Interest- bearing liabilities									
Deposits of the public									
In Israel	**245,876**	**(2,963)**	**(1.21)**	244,151	(4,190)	(1.72)	226,089	(4,836)	(2.14)
On demand	**63,679**	**(127)**	**(0.20)**	49,734	(177)	(0.36)	46,608	(211)	(0.45)
Fixed term	**182,197**	**(2,836)**	**(1.56)**	194,417	(4,013)	(2.06)	179,481	(4,625)	(2.58)
Outside Israel	**18,348**	**(186)**	**(1.01)**	18,525	(251)	(1.35)	16,512	(349)	(2.11)
On demand	**3,395**	**(11)**	**(0.32)**	2,748	(19)	(0.69)	3,709	(8)	(0.22)
Fixed term	**14,953**	**(175)**	**(1.17)**	15,777	(232)	(1.47)	12,803	(341)	(2.66)
Total	**264,224**	**(3,149)**	**(1.19)**	262,676	(4,441)	(1.69)	242,601	(5,185)	(2.14)
Deposits of the government									
In Israel	**224**	**(8)**	**(3.57)**	316	(14)	(4.43)	431	(22)	(5.10)
Outside Israel	**233**	**-**	**-**	141	-	-	141	-	-
Total	**457**	**(8)**	**(1.75)**	457	(14)	(3.06)	572	(22)	(3.85)
Deposits from central banks									
In Israel	**-**	**-**	**-**	-	-	-	226	-	-
Outside Israel	**-**	**-**	**-**	-	-	-	-	-	-
Total	**-**	**-**	**-**	-	-	-	226	-	-
Deposits from banks									
In Israel	**3,408**	**(35)**	**(1.03)**	2,460	(50)	(2.03)	2,910	(94)	(3.23)
Outside Israel	**195**	**(2)**	**(1.03)**	848	(8)	(0.94)	1,220	(32)	(2.62)
Total	**3,603**	**(37)**	**(1.03)**	3,308	(58)	(1.75)	4,130	(126)	(3.05)
Securities lent or sold under resale agreements									
In Israel	**728**	**(13)**	**(1.79)**	1,028	(29)	(2.82)	859	(27)	(3.14)
Outside Israel	**28**	**(1)**	**(3.57)**	58	(2)	(3.45)	268	(3)	(1.12)
Total	**756**	**(14)**	**(1.85)**	1,086	(31)	(2.85)	1,127	(30)	(2.66)
Bonds									
In Israel	**26,884**	**(1,568)**	**(5.83)**	27,927	(1,550)	(5.55)	26,670	(1,873)	(7.02)
Outside Israel	**10**	**(1)**	**(10.00)**	434	(5)	(1.15)	897	60	6.69
Total	**26,894**	**(1,569)**	**(5.83)**	28,361	(1,555)	(5.48)	27,567	(1,813)	(6.58)
Total interest-bearing liabilities	**295,934**	**(4,777)**	**(1.61)**	295,888	(6,099)	(2.06)	276,223	(7,176)	(2.60)
Non-interest bearing deposits of the public	**13,833**			14,190			10,038		
Payables for non-interest bearing credit cards	**7,565**			6,606			6,616		
Other non-interest bearing liabilities [7]	**23,419**			21,772			19,941		
Total liabilities	**340,751**	**(4,777)**		338,456	(6,099)		312,818	(7,176)	
Total capital means	**25,658**			24,459			22,858		
Total liabilities and capital means	**366,409**	**(4,777)**		362,915	(6,099)		335,676	(7,176)	
Interest margin	**-**	**7,357**	**2.08**	-	7,408	2.08	-	7,107	2.12
Net yield[8] on income-bearing assets									
In Israel	**291,731**	**6,504**	**2.23**	286,493	6,432	2.25	269,591	6,255	2.32
Outside Israel	**36,823**	**853**	**2.32**	39,435	976	2.47	33,038	852	2.58
Total	**328,554**	**7,357**	**2.24**	325,928	7,408	2.27	302,629	7,107	2.35
Total income-bearing liabilities attributable to activity outside Israel	**18,814**	**(190)**	**(1.01)**	20,006	(266)	(1.33)	19,038	(324)	(1.70)

See notes on page 275 below.

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

Rates of income and expenses[1] and analysis of changes in interest income and expenses (cont'd)

Exhibit C (cont'd)

Part C – Average balances and interest rates – additional information on interest-bearing assets and liabilities related to activity in Israel

	2013			2012			2011		
	Average balance[2]	Interest income (expenses)	Rate of income (expenses)	Average balance[2]	Interest income (expenses)	Rate of income (expenses)	Average balance[2]	Interest income (expenses)	Rate of income (expenses)
	(NIS millions)		%	(NIS millions)		%	(NIS millions)		%
Index-linked Israeli currency									
Total interest-bearing assets	**59,248**	**3,203**	**5.41**	62,038	3,181	5.13	60,571	3,669	6.06
Total interest-bearing liabilities	**49,692**	**(2,581)**	**(5.19)**	49,875	(2,423)	(4.86)	48,101	(2,993)	(6.22)
Interest margin	**9,556**	**622**	**0.22**	12,163	758	0.27	12,470	676	(0.16)
Unlinked Israeli currency									
Total interest-bearing assets	**189,437**	**6,978**	**3.68**	178,298	7,980	4.48	160,414	8,007	4.99
Total interest-bearing liabilities	**153,262**	**(1,752)**	**(1.14)**	150,262	(2,835)	(1.89)	137,846	(3,050)	(2.21)
Interest margin	**36,175**	**5,226**	**2.54**	28,036	5,145	2.59	22,568	4,957	2.78
Foreign currency									
Total interest-bearing assets	**43,046**	**910**	**2.11**	46,157	1,104	2.39	48,606	1,431	2.94
Total interest-bearing liabilities	**74,166**	**(254)**	**(0.34)**	75,745	(575)	(0.76)	71,238	(809)	(1.14)
Interest margin	**(31,120)**	**656**	**1.77**	(29,588)	529	1.63	(22,632)	622	1.80
Total activity in Israel									
Total interest-bearing assets	**291,731**	**11,091**	**3.80**	286,493	12,265	4.28	269,591	13,107	4.86
Total interest-bearing liabilities	**277,120**	**(4,587)**	**(1.66)**	275,882	(5,833)	(2.11)	257,185	(6,852)	(2.66)
Interest margin	**14,611**	**6,504**	**2.14**	10,611	6,432	2.17	12,406	6,255	2.20

See notes on page 275 below.

Bank Leumi le-Israel B.M. and its Consolidated Companies
Rates of income and expenses[1] and analysis of changes in interest income and expenses (cont'd)

Exhibit C (cont'd)

Part D – Analysis of changes in interest income and interest expenses

	2013 compared to 2012			2012 compared to 2011		
	Increase (decrease) due to change[9]		Net change	Increase (decrease) due to change[9]		Net change
	Amount	Price		Amount	Price	
	(NIS millions)					
Interest-bearing assets						
Credit to the public						
In Israel	(1)	(759)	(760)	472	(1,178)	(706)
Outside Israel	(65)	(75)	(140)	118	29	147
Total	(66)	(834)	(900)	590	(1,149)	(559)
Other interest-bearing assets						
In Israel	89	(503)	(414)	175	(311)	(136)
Outside Israel	(5)	(54)	(59)	36	(117)	(81)
Total	84	(557)	(473)	211	(428)	(217)
Total interest income	18	(1,391)	(1,373)	801	(1,577)	(776)
Interest-bearing liabilities						
Deposits of the public						
In Israel	21	(1,248)	(1,227)	310	(956)	(646)
Outside Israel	(3)	(62)	(65)	26	(124)	(98)
Total	18	(1,310)	(1,292)	336	(1,080)	(744)
Other interest-bearing liabilities						
In Israel	(25)	6	(19)	33	(406)	(373)
Outside Israel	(9)	(2)	(11)	(11)	51	40
Total	(34)	4	(30)	22	(355)	(333)
Total interest expenses	(16)	(1,306)	(1,322)	358	(1,435)	(1,077)

Exhibit C (cont'd)

Notes:

(1) The data in these tables are after the effect of derivative instruments.

(2) Based on monthly opening balances, except for the unlinked Israeli currency sector in which the average balance is based on daily figures.

(3) Before deduction of the average balance of allowances for credit losses. Including impaired debts not accruing interest income.

(4) From the average balance of the assets there has been deducted (added) the average balance of unrealized profits (losses) from adjustments to fair value of debentures held for trading and available for sale, as follows:

In the unlinked Israeli currency sector - the amount of NIS 106 million (31 December 2012 – NIS 107 million).

In the index-linked Israeli currency sector – the amount of NIS 71 million (31 December 2012 – NIS 73 million).

In the foreign currency sector (including Israeli currency linked to foreign currency), the amount of NIS 226 million (31 December 2012 – NIS (23) million).

(5) From the average balance of the assets there has been deducted (added) the balance of unrealized profits (losses) from adjustments to fair value of debentures held for trading and available for sale, in the amount of NIS 403 million in the various sectors (31 December 2012 – NIS 157 million).

(6) Including book balances of derivative instruments, other non-interest bearing assets, non-monetary assets and after deducting the allowance for credit losses.

(7) Including book balances of derivative instruments, and non-monetary liabilities.

(8) Net return – net interest income divided by total interest-bearing assets.

(9) The calculation of the allocation between a change in amount and a change in price is made as follows: change in price - the change in price is multiplied by the book balance for the corresponding period; change in amount – the change in book balance is multiplied by the price for the current period.

(10) Commissions in the amount of NIS 273 million were included in interest income from credit to the public (31 December 2012 – NIS 227 million).

Bank Leumi le-Israel B.M. and its Consolidated Companies
Exposure to Interest Rate Fluctuations
Exhibit D

	31 December 2013												31 December 2012		
	On demand up to one month	Over one month to three months	Over three months to one year	Over one year to three years	Over three years to five years	Over five years to ten years	Over ten years to twenty years	Over twenty years	Without fixed maturity	Total	Internal rate of return	Average duration (2)	Total fair value	Internal rate of return	Average duration (2)
	NIS millions										(%)	(Years)		(%)	(Years)
Israeli currency - unlinked															
Financial assets, amounts receivable in respect of derivative instruments and off-balance sheet financial instruments															
Financial assets (1)	150,164	8,388	33,352	7,843	4,882	4,410	1,821	79	300	211,239	3.51	0.59	204,561	3.95	0.45
Derivative financial instruments (excluding options)	54,755	100,802	41,616	43,134	29,922	32,290	636	-	-	303,155	-	1.63	269,939	-	1.53
Options (in terms of the underlying asset) (4)	4,171	1,249	1,231	28	192	1,605	18	-	-	8,494	-	-	10,835	-	-
Off-balance sheet financial instruments	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Total fair value	209,090	110,439	76,199	51,005	34,996	38,305	2,475	79	300	522,888	3.51	1.19	485,335	3.95	1.04
Financial liabilities, amounts payable in respect of derivative instruments and off-balance sheet financial instruments															
Financial liabilities (1)	147,285	8,598	5,650	4,885	3,212	305	31	-	8	169,974	0.93	0.23	168,101	2.65	0.25
Derivative financial instruments (excluding options)	66,182	110,398	40,517	47,950	31,200	31,631	606	26	-	328,510	-	1.56	288,807	-	1.44
Options (in terms of the underlying asset) (4)	2,832	1,061	1,229	660	8	61	17	-	-	5,868	-	-	11,390	-	-
Off-balance sheet financial instruments	-	-	27	-	-	-	-	-	-	27	-	0.50	34	-	0.50
Total fair value	216,299	120,057	47,423	53,495	34,420	31,997	654	26	8	504,379	0.93	1.10	468,332	2.65	0.98
Financial instruments, net															
Exposure to interest rate fluctuations	(7,209)	(9,618)	28,776	(2,490)	576	6,308	1,821	53							
Accumulated exposure in the sector	(7,209)	(16,827)	11,949	9,459	10,035	16,343	18,164	18,217							
Israeli currency – linked to the CPI															
Financial assets, amounts receivable in respect of derivative instruments and off-balance sheet financial instruments															
Financial assets (1)	2,432	3,078	13,160	17,101	15,894	6,941	1,286	61	7	59,960	2.03	2.93	62,635	2.29	2.84
Derivative financial instruments (excluding options)	713	82	1,877	1,279	1,561	1,586	-	-	-	7,098	-	3.03	5,874	-	2.53
Options (in terms of the underlying asset) (4)	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Off-balance sheet financial instruments	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Total fair value	3,145	3,160	15,037	18,380	17,455	8,527	1,286	61	7	67,058	2.03	2.94	68,509	2.29	2.81
Financial liabilities, amounts payable in respect of derivative instruments and off-balance sheet financial instruments															
Financial liabilities (1)	1,642	2,508	9,542	17,039	9,564	11,976	885	269	-	53,425	1.27	3.36	54,421	1.43	3.57
Derivative financial instruments (excluding options)	431	1,264	3,788	1,626	909	1,385	341	-	-	9,744	-	2.47	12,531	-	1.97
Options (in terms of the underlying asset) (4)	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Off-balance sheet financial instruments	-	-	100	-	-	-	-	-	-	100	-	-	101	-	-
Total fair value	2,073	3,772	13,430	18,665	10,473	13,361	1,226	269	-	63,269	1.27	3.21	67,053	1.43	3.26
Financial instruments, net															
Exposure to interest rate fluctuations	1,072	(612)	1,607	(285)	6,982	(4,834)	60	(208)							
Accumulated exposure in the sector	1,072	460	2,067	1,782	8,764	3,930	3,990	3,782							

See notes on page 278.

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

Exposure to Interest Rate Fluctuations (cont'd)

Exhibit D (cont'd)

	31 December 2013												31 December 2012		
	On demand up to one month	Over one month to three months	Over three months to one year	Over one year to three years	Over three years to five years	Over five years to ten years	Over ten years to twenty years	Over twenty years	Without fixed maturity	Total	Internal rate of return	Average duration (2)	Total fair value	Internal rate of return	Average duration (2)
	NIS millions										(%)	(Years)		(%)	(Years)
Foreign currency and foreign currency linked															
Financial assets, amounts receivable in respect of derivative instruments and off-balance sheet financial instruments															
Financial assets (1)	40,771	14,838	5,675	7,455	4,455	3,922	402	86	196	77,800	2.40	0.99	86,455	1.90	0.80
Derivative financial instruments (excluding options)	50,564	60,675	32,591	8,392	5,465	9,741	530	19	150	168,127	-	0.87	163,552	-	0.81
Options (in terms of the underlying asset) (4)	2,427	3,060	2,783	530	4,411	533	40	-	-	13,784	-	-	10,607	-	-
Off-balance sheet financial instruments	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Total fair value	93,762	78,573	41,049	16,377	14,331	14,196	972	105	346	259,711	2.40	0.86	260,614	1.90	0.78
Financial liabilities, amounts payable in respect of derivative instruments and off-balance sheet financial instruments															
Financial liabilities (1)	73,916	12,760	13,788	3,282	681	451	25	-	17	104,920	0.86	0.27	111,529	1.09	0.28
Derivative financial instruments (excluding options)	38,349	43,352	28,982	10,605	7,059	11,719	594	43	150	140,853	-	1.17	139,465	-	1.08
Options (in terms of the underlying asset) (4)	3,213	2,685	2,786	544	4,574	1,927	40	-	-	15,769	-	-	9,974	-	-
Off-balance sheet financial instruments	-	-	14	-	-	-	-	-	-	14	-	0.50	9	-	0.50
Total fair value	115,478	58,797	45,570	14,431	12,314	14,097	659	43	167	261,556	0.86	0.74	260,977	1.09	0.70
Financial instruments, net															
Exposure to interest rate fluctuations	(21,716)	19,776	(4,521)	1,946	2,017	99	313	62							
Accumulated exposure in the sector	(21,716)	(1,940)	(6,461)	(4,515)	(2,498)	(2,399)	(2,086)	(2,024)							
Total exposure to interest rate fluctuations															
Financial assets, amounts receivable in respect of derivative instruments and off-balance sheet financial instruments															
Financial assets (1) (3)	193,367	26,304	52,187	32,399	25,231	15,273	3,509	226	4,936	353,432	2.62	1.08	356,648	2.68	0.96
Derivative financial instruments (excluding options)	106,032	161,559	76,084	52,805	36,948	43,617	1,166	19	1,713	479,943	-	1.39	439,665	-	1.28
Options (in terms of the underlying asset) (4)	6,598	4,309	4,014	558	4,603	2,138	58	-	16	22,294	-	-	21,442	-	-
Off-balance sheet financial instruments	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Total fair value	305,997	192,172	132,285	85,762	66,782	61,028	4,733	245	6,665	855,669	2.62	1.23	817,755	2.68	1.11
Financial liabilities, amounts payable in respect of derivative instruments and off-balance sheet financial instruments															
Financial assets (1) (3)	222,843	23,866	28,980	25,206	13,457	12,732	941	269	666	328,960	1.46	0.75	334,690	1.59	0.80
Derivative financial instruments (excluding options)	104,962	155,014	73,287	60,181	39,168	44,735	1,541	69	2,076	481,033	-	1.47	441,067	-	1.34
Options (in terms of the underlying asset) (4)	6,045	3,746	4,015	1,204	4,582	1,988	57	-	-	21,637	-	-	21,364	-	-
Off-balance sheet financial instruments	-	-	141	-	-	-	-	-	148	289	-	0.09	283	-	0.09
Total fair value	333,850	182,626	106,423	86,591	57,207	59,455	2,539	338	2,890	831,919	1.46	1.14	797,404	1.59	1.08
Financial instruments, net															
Exposure to interest rate fluctuations	(27,853)	9,546	25,862	(829)	9,575	1,573	2,194	(93)							
Accumulated exposure in the sector	(27,853)	(18,307)	7,555	6,726	16,301	17,874	20,068	19,975							

See notes on next page.

Notes:

(1) Excluding book balances of derivative financial instruments, fair value of off-balance sheet financial instruments, and fair value of complex financial instruments. In the "Without fixed maturity" column are reported non-discounted book balances. Including balances after their repayment date in the amount of NIS 496 million.
(2) Weighted average according to fair value of effective duration.
(3) Including non-monetary items shown in the "Without fixed maturity" column.
(4) Duration less than 0.05 years.

General notes:

(1) In this table, the data by periods represent the present value of future cash flows, discounted at the internal rate of return used for discounting to the fair value included in respect of the financial instrument, consistent with the assumptions used in calculating the fair value of the financial instrument. For further details regarding the assumptions used in the calculation of the fair value of the financial instruments, see Note 18 in the Annual Financial Report.
(2) The internal rate of return is the interest rate for discounting the cash flows expected from a financial instrument to the fair value included in respect of it.
(3) The effective duration of a group of financial instruments constitutes an approximation of the percentage change in the fair value of the group of financial instruments that would be caused as a result of a small change (an increase of 0.1%) in the internal rate of return of each of the financial instruments.
(4) The effect of hedging transactions is included in total assets or total liabilities, as applicable.
(5) In calculating the duration of assets and liabilities in the CPI-linked segment an estimate was taken into account of early redemptions and withdrawals at exit points in savings plans, in accordance with a model estimating expected early redemptions based on the behavior of savers. The duration of total assets according to the original cash flow of the savings plans is higher and reached 3.35 years, the duration of total liabilities reaches 3.31 years, and the gap in the internal rate of return (hereinafter – IRR) amounts to 0.52%. The change in fair value in total assets is NIS 553 million and in total liabilities NIS (1) million.
(6) Further details of the exposure to interest rate fluctuations for each segment of financial assets and financial liabilities by the various balance sheet headings, will be supplied on request.

Bank Leumi le-Israel B.M. and its Consolidated Companies
Overall credit risk to the public by sector of the economy
Exhibit E

	31 December 2013								
	Overall credit risk[1]		Debts[2] and off-balance sheet credit risk (excluding derivatives)[3]						
							Credit losses[4]		
				*Of which:					
Activities of borrowers in Israel	Total	Problematic[5]	Total(*)	Debts[2]	Problematic[5]	Impaired	Expenses in respect of credit losses	Net accounting write-offs	Balance of allowance for credit losses
	(NIS millions)								
Agriculture	2,125	113	2,116	1,823	113	51	-	(5)	(45)
Industry	29,219	2,256	27,673	18,592	2,218	580	36	8	(523)
Construction and real estate - construction	41,188	1,687	41,096	14,720	1,667	574	(59)	(19)	(386)
Construction and real estate - real estate activity	25,758	1,706	25,650	23,374	1,703	1,416	(44)	(21)	(546)
Electricity and water	4,471	1	3,876	3,530	1	1	(11)	-	(4)
Commerce	22,400	1,123	21,995	18,144	1,122	525	(27)	102	(351)
Hotels, accomodation and food services	2,924	316	2,887	2,622	316	233	(14)	(6)	(26)
Transport and storage	5,805	532	5,738	5,005	522	314	(28)	5	(92)
Communications and computer services	5,045	131	4,855	3,812	131	119	11	(6)	(76)
Financial services	29,901	675	19,580	11,136	665	346	(118)	240	(224)
Other business services	8,258	153	8,158	6,362	153	123	5	16	(83)
Public and community services	7,451	56	7,413	6,109	56	14	18	13	(13)
Total commercial	184,545	8,749	171,037	115,229	8,667	4,296	(231)	327	(2,369)
Private individuals - housing loans	70,787	803	70,787	68,592	803	-	46	22	(479)
Private individuals - other	61,782	418	61,747	31,458	418	109	177	73	(456)
Total public	317,114	9,970	303,571	215,279	9,888	4,405	(8)	422	(3,304)
Israeli banks	7,509	-	1,890	1,688	-	-	1	-	(1)
Government of Israel	39,536	-	338	338	-	-	-	-	-
Total activity in Israel	364,159	9,970	305,799	217,305	9,888	4,405	(7)	422	(3,305)

	31 December 2013								
	Overall credit risk[1]		Debts[2] and off-balance sheet credit risk (excluding derivatives)[3]						
							Credit losses[4]		
				*Of which:					
Activities of borrowers abroad	Total	Problematic[5]	Total(*)	Debts[2]	Problematic[5]	Impaired	Expenses in respect of credit losses	Net accounting write-offs	Balance of allowance for credit losses
	(NIS millions)								
Agriculture	62	4	57	48	4	5	(2)	-	(1)
Industry	9,526	447	8,569	5,764	447	331	57	16	(230)
Construction and real estate - construction	11,400	891	10,671	7,667	891	724	82	10	(386)
Electricity and water	411	-	175	37	-	-	-	-	-
Commerce	7,851	234	7,761	5,337	234	200	18	6	(125)
Hotels, accomodation and food services	1,900	212	1,899	1,847	212	45	28	18	(13)
Transport and storage	491	27	358	347	27	26	-	(1)	(15)
Communications and computer services	636	-	438	138	-	-	-	-	(2)
Financial services	17,211	94	3,450	2,344	92	74	3	27	(36)
Other business services	2,995	198	2,781	1,947	198	197	70	3	(109)
Public and community services	2,118	2	2,004	1,767	2	2	5	(1)	(15)
Total commercial	54,601	2,109	38,163	27,243	2,107	1,604	261	78	(932)
Private individuals - housing loans	1,198	69	1,198	1,198	69	49	7	7	(19)
Private individuals - other	1,281	41	1,249	1,037	41	41	5	7	(40)
Total public	57,080	2,219	40,610	29,478	2,217	1,694	273	92	(991)
Foreign banks	32,646	-	14,408	13,016	-	-	2	5	(1)
Foreign governments	5,190	-	318	220	-	-	-	-	-
Total activity abroad	94,916	2,219	55,336	42,714	2,217	1,694	275	97	(992)
Total	459,075	12,189	361,135	260,019	12,105	6,099	268	519	(4,297)

(1) Balance sheet credit risk and off-balance sheet credit risk, including in respect of derivative instruments, including debts[2], bonds, securities borrowed or purchased under agreements to resell, assets in respect of derivative instruments, and credit risk in off-balance sheet financial instruments as calculated for single borrower debt limitations in the sum of NIS 260,019, 59,816, 1,360, 12,969, 124,911 million, respectively.

(2) Credit risk to the public, credit to governments, deposits with banks (in 2013 except for deposits in the Bank of Israel) and other debts, except for bonds and securities borrowed or purchased under agreements to resell.

(3) Credit risk of off-balance sheet financial instruments as calculated for the purpose of single borrower debt limitations.

(4) Including in respect of off-balance sheet credit instruments (shown in the balance sheet under "Other liabilities").

(5) Impaired, substandard, or special mention balance sheet credit risk, including in respect of housing loans for which there is a provision by extent of arrears, and housing loans for which there is no provision by extent of arrears that are in arrears of 90 days or more.

Bank Leumi le-Israel B.M. and its Consolidated Companies
Overall credit risk to the public by sector of the economy (cont'd)

Exhibit E (cont'd)

	31 December 2012								
	Overall credit risk[1]		Debts[2] and off-balance sheet credit risk (excluding derivatives)[3]						
							Credit losses[4]		
				*Of which:					
Activities of borrowers in Israel	Total	Problematic[5]	Total(*)	Debts[2]	Problematic[5]	Impaired	Expenses in respect of credit losses	Net accounting write-offs	Balance of allowance for credit losses
	(NIS millions)								
Agriculture	2,043	102	2,032	1,729	102	40	(11)	(15)	(43)
Industry	32,841	2,259	31,024	20,467	2,175	805	201	137	(586)
Construction and real estate - construction	40,387	1,368	40,272	14,261	1,368	905	(120)	79	(404)
Construction and real estate - real estate activity	28,233	2,276	28,169	25,541	2,274	1,887	88	173	(498)
Electricity and water	3,313	8	2,427	2,054	8	8	-	1	(3)
Commerce	22,179	1,325	21,668	17,955	1,320	768	195	43	(479)
Hotels, accomodation and food services	3,033	301	3,007	2,758	301	210	(59)	14	(26)
Transport and storage	5,954	894	5,873	5,034	868	373	53	13	(147)
Communications and computer services	5,778	86	5,549	4,602	86	31	(47)	(15)	(38)
Financial services	28,429	1,190	21,219	13,217	1,155	758	576	263	(520)
Other business services	8,094	200	7,939	6,274	200	159	13	2	(156)
Public and community services	7,646	192	7,602	6,336	192	154	40	60	(25)
Total commercial	187,930	10,201	176,781	120,228	10,049	6,098	929	755	(2,925)
Private individuals - housing loans	64,136	860	64,137	62,101	860	1	(13)	47	(455)
Private individuals - other	57,415	352	57,406	28,941	352	47	91	165	(351)
Total public	309,481	11,413	298,324	211,270	11,261	6,146	1,007	967	(3,731)
Israeli banks	45,091	-	39,295	38,478	-	-	-	-	-
Government of Israel	33,694	-	282	282	-	-	-	-	-
Total activity in Israel	388,266	11,413	337,901	250,030	11,261	6,146	1,007	967	(3,731)

	31 December 2012								
	Overall credit risk[1]		Debts[2] and off-balance sheet credit risk (excluding derivatives)[3]						
							Credit losses[4]		
				*Of which:					
Activities of borrowers abroad	Total	Problematic[5]	Total(*)	Debts[2]	Problematic[5]	Impaired	Expenses in respect of credit losses	Net accounting write-offs	Balance of allowance for credit losses
	(NIS millions)								
Agriculture	81	9	64	50	9	9	1	-	(3)
Industry	11,225	326	10,249	7,025	323	277	98	16	(184)
Construction and real estate	11,409	1,092	10,754	8,375	1,092	878	135	65	(315)
Electricity and water	370	-	164	32	-	-	-	-	-
Commerce	9,082	231	8,933	6,156	231	177	(1)	3	(136)
Hotels, accomodation and food services	2,296	73	2,295	2,106	73	56	-	18	(11)
Transport and storage	456	49	442	400	49	29	(1)	(2)	(14)
Communications and computer services	644	-	437	260	-	-	(1)	-	(2)
Financial services	15,081	47	4,747	3,619	47	21	(8)	51	(27)
Other business services	3,246	218	3,143	2,349	218	217	2	23	(61)
Public and community services	1,505	13	1,391	1,040	13	7	2	-	(13)
Total commercial	55,395	2,058	42,619	31,412	2,055	1,671	227	174	(766)
Private individuals - housing loans	1,303	47	1,303	1,302	47	43	-	-	(20)
Private individuals - other	1,685	52	1,646	1,394	52	51	2	1	(44)
Total public	58,383	2,157	45,568	34,108	2,154	1,765	229	175	(830)
Foreign banks	33,728	5	18,343	14,008	5	5	-	1	(4)
Foreign governments	7,065	-	300	160	-	-	-	-	-
Total activity abroad	99,176	2,162	64,211	48,276	2,159	1,770	229	176	(834)
Total	487,442	13,575	402,112	298,306	13,420	7,916	1,236	1,143	(4,565)

(1) Balance sheet credit risk and off-balance sheet credit risk, including in respect of derivative instruments, including debts[2], bonds, securities borrowed or purchased under agreements to resell, assets in respect of derivative instruments, and credit risk in off-balance sheet financial instruments as calculated for single borrower debt limitations in the sum of NIS 298,306, 54,042, 1,435, 11,438, 122,221 million, respectively.

(2) Credit risk to the public, credit to governments, deposits with banks and other debts, except for bonds and securities borrowed or purchased under agreements to resell.

(3) Credit risk of off-balance sheet financial instruments as calculated for the purpose of single borrower debt limitations.

(4) Including in respect of off-balance sheet credit instruments (shown in the balance sheet under "Other liabilities").

(5) Impaired, substandard, or special mention balance sheet credit risk, including in respect of housing loans for which there is a provision by extent of arrears, and housing loans for which there is no provision by extent of arrears that are in arrears of 90 days or more.

Bank Leumi le-Israel B.M. and its Consolidated Companies
Exposure to Foreign Countries

Exhibit F

Part A – Information on total exposure to foreign countries and on exposure to countries whose total individual exposure exceeds 1% of total assets or exceeds 20% of total equity for purposes of calculating capital ratios, whichever the lower.

	31 December 2013					
	Balance sheet exposure (1)					
	Cross-Border Balance Sheet Exposure			Balance sheet exposure of foreign offices of the banking corporation to local residents		
	To governments (3)	To banks	To others	Balance sheet exposure before deducting local liabilities	Deduction for local liabilities	Net balance sheet exposure after deducting local liabilities
Country	NIS millions					
United States	3,092	5,074	10,340	16,219	8,365	7,854
United Kingdom	457	3,702	3,552	7,433	2,188	5,245
France	-	1,957	839	-	-	-
Switzerland	-	378	757	2,238	463	1,775
Germany	-	2,783	2,262	-	-	-
Belgium	427	129	144	-	-	-
Italy	-	264	64	-	-	-
Netherlands	-	847	1,533	-	-	-
Others	290	2,306	3,027	2,237	770	1,467
Total exposure to foreign countries	4,266	17,440	22,518	28,127	11,786	16,341
Total exposure to LDC countries	149	680	1,143	1,605	735	870
Total exposure to GIIPS countries (4)	-	278	491	-	-	-

	31 December 2013						
	Balance sheet Exposure			Off-balance sheet exposure (1)(2)			
						Cross-Border Balance Sheet Exposure	
						Repayment period	
	Total balance sheet exposure	Balance sheet problem credit risk	Of which: Balance of impaired debts	Total off-balance sheet exposure	Of which: Off-balance sheet problem credit risk	Up to one year	Over one year
Country	NIS millions						
United States	26,360	522	390	9,243	16	6,160	12,346
United Kingdom	12,956	750	581	5,543	-	3,595	4,116
France	2,796	9	1	1,923	-	1,001	1,795
Switzerland	2,910	21	21	773	-	862	273
Germany	5,045	161	-	1,028	-	3,305	1,740
Belgium	700	-	-	183	-	302	398
Italy	328	-	-	35	-	145	183
Netherlands	2,380	55	47	139	-	1,182	1,198
Others	7,090	523	489	1,459	-	4,339	1,284
Total exposure to foreign countries	60,565	2,041	1,529	20,326	16	20,891	23,333
Total exposure to LDC countries	2,842	508	480	1,072	-	1,708	264
Total exposure to GIIPS countries (4)	769	-	-	70	-	462	307

See notes on next page.

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

Exposure to Foreign Countries (cont'd)

Exhibit F (cont'd)

Part A – Information on total exposure to foreign countries and on exposure to countries whose total individual exposure exceeds 1% of total assets or exceeds 20% of total equity for purposes of calculating capital ratios, whichever the lower (cont'd).

	31 December 2012					
	Balance sheet exposure (1)					
	Cross-Border Balance Sheet Exposure			Balance sheet exposure of foreign offices of the banking corporation to local residents		
	To governments (3)	To banks	To others	Balance sheet exposure before deducting local liabilities	Deduction for local liabilities	Net balance sheet exposure after deducting local liabilities
Country	NIS millions					
United States	5,472	4,161	8,519	17,965	10,201	7,764
United Kingdom	121	3,849 (5)	3,147 (5)	6,907	2,268	4,639
France	-	2,225	679	-	-	-
Switzerland	-	423	1,040	2,463	373	2,090
Germany	395	1,711	1,960	-	-	-
Belgium	-	172	131	-	-	-
Italy	-	255	93	-	-	-
Netherlands	-	1,425	1,638	-	-	-
Others	368	3,020	2,657	1,947	1,007	940
Total exposure to foreign countries	6,356	17,241	19,864	29,282	13,849	15,433
Total exposure to LDC countries	187	613	1,225	1,920	986	934
Total exposure to GIIPS countries (4)	-	344	217	-	-	-

	31 December 2012						
	Balance sheet Exposure			Off-balance sheet exposure (1)(2)			
						Cross-Border Balance Sheet Exposure	
						Repayment period	
	Total balance sheet exposure	Balance sheet problem credit risk	Of which: Balance of impaired debts	Total off-balance sheet exposure	Of which: Off-balance sheet problem credit risk	Up to one year	Over one year
	NIS millions						
Country							
United States	25,916	512	330	7,391	16	7,813	10,339
United Kingdom	11,756	621	484	5,041	4	2,677	4,440
France	2,904	1	1	1,398	-	1,391	1,513
Switzerland	3,553	37	37	1,021	-	1,117	346
Germany	4,066	3	3	1,030	-	2,180	1,886
Belgium	303	-	-	200	-	268	35
Italy	348	1	1	35	-	96	252
Netherlands	3,063	51	34	161	-	2,117	946
Others	6,985	569	528	1,379	-	4,779	1,266
Total exposure to foreign countries	58,894	1,795	1,418	17,656	20	22,438	21,023
Total exposure to LDC countries	2,959	559	518	780	-	1,737	288
Total exposure to GIIPS countries (4)	561	1	1	40	-	163	398

(1) Balance sheet credit risk and off-balance sheet credit risk, problematic commercial credit risk and impaired debts are shown before the effect of the allowance for credit losses and before the effect of collateral deductible for purposes of single borrower and group borrower debt limitations. Does not include off-balance sheet risk components.
(2) Credit risk of off-balance sheet financial instruments as calculated for the purpose of single borrower debt limitations.
(3) Including governments, official institutions and central banks.
(4) Exposure to GIIPS countries include: Portugal, Ireland, Italy, Greece and Spain.
(5) Reclassified.
(6) Restated.

Exhibit F (cont'd)

In accordance with the Directive of the Supervisor of Banks, exposure to foreign countries 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 bearing 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 calculated for purposes of single borrower debt limitations.

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 – On 31 December 2013 and 31 December 2012, there was no aggregate amount of balance sheet exposure to foreign countries whose total individual exposure was between 0.75% and 1% of the total consolidated assets or between 15% and 20% of equity, whichever the lower.

Part C – The amount of exposure to foreign countries with liquidity problems as defined by the Bank of Israel (a country receiving financial aid from the IMF or whose obligations are rated with a credit rating of CCC or lower) amounts to NIS 1,803 million and relates to 13 countries (at 31 December 2012, this totaled NIS 1,317 million and related to 14 countries).

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

Quarterly Consolidated Balance Sheets – Multi-Quarter Data

Exhibit G

Year	2013				2012			
Quarter	4	3	2	1	4	3	2	1
	(NIS millions)							
Assets								
Cash and deposits with banks	44,351	40,202	42,754	53,933	54,621	48,340	39,166	47,368
Securities	63,735	60,984	57,580	53,378	56,408	56,183	60,348	49,757
Securities borrowed or purchased under agreements to resell	1,360	1,098	1,973	854	1,435	1,946	2,165	1,485
Credit to the public	244,757	244,736	242,425	242,695	245,378	245,407	245,287	244,575
Allowance for credit losses	(3,883)	(3,844)	(3,942)	(4,081)	(4,114)	(3,943)	(3,860)	(4,075)
Credit to the public, net	240,874	240,892	238,483	238,614	241,264	241,464	241,427	240,500
Credit to governments	558	533	478	423	442	418	412	425
Investments in companies included on equity basis	1,689	1,944	1,978	2,122	2,129	2,303	2,129	2,187
Buildings and equipment	3,638	3,647	3,639	3,685	3,705	3,751	3,753	3,715
Intangible assets and goodwill	99	103	182	185	189	168	172	176
Assets in respect of derivative instruments	13,054	10,966	11,915	11,839	11,438	10,494	12,259	9,466
Other assets	5,002	5,053	4,732	4,496	4,529	4,463	4,251	4,189
Total assets	374,360	365,422	363,714	369,529	376,160	369,530	366,082	359,268
Liabilities and equity								
Deposits of the public	286,003	279,839	275,448	278,820	289,538	285,229	280,434	277,642
Deposits from banks	4,310	3,805	4,245	7,579	4,073	2,863	3,981	3,629
Deposits from governments	397	437	455	473	451	456	462	436
Securities loaned or sold under agreements to repurchase	624	404	1,327	735	1,007	1,248	1,287	624
Debentures, bonds and subordinated notes	25,441	25,596	27,587	27,542	27,525	28,189	28,223	27,873
Liabilities in respect of derivative instruments	13,487	12,078	12,656	12,879	12,762	11,259	12,575	10,125
Other liabilities	17,333	16,851	16,101	15,909	15,576	14,967	14,587	14,564
Total liabilities	347,595	339,010	337,819	343,937	350,932	344,211	341,549	334,893
Non-controlling interests	340	331	318	308	307	301	267	257
Equity attributable to shareholders of the banking corporation	26,425	26,081	25,577	25,284	24,921	25,018	24,266	24,118
Total equity	26,765	26,412	25,895	25,592	25,228	25,319	24,533	24,375
Total liabilities and equity	374,360	365,422	363,714	369,529	376,160	369,530	366,082	359,268

Bank Leumi le-Israel B.M. and its Consolidated Companies
Quarterly Consolidated Statements of Profit and Loss – Multi-Quarter Data

Exhibit H

Year	2013				2012			
Quarter	4	3	2	1	4	3	2	1
	(NIS millions)							
Interest income	**2,614**	**3,466**	**3,191**	**2,863**	2,714	3,615	3,914	3,264
Interest expenses	**804**	**1,520**	**1,352**	**1,101**	930	1,743	1,990	1,436
Interest income, net	**1,810**	**1,946**	**1,839**	**1,762**	1,784	1,872	1,924	1,828
Expenses in respect of credit losses	**155**	**(44)**	**84**	**73**	386	292	333	225
Net interest income after expenses in respect of credit losses	**1,655**	**1,990**	**1,755**	**1,689**	1,398	1,580	1,591	1,603
Non-interest income								
Non-interest financing income	**238**	**266**	**212**	**411**	205	119	(25)	145
Commissions	**1,084**	**1,050**	**1,029**	**1,025**	1,107	1,050	1,022	1,020
Other income	**98**	**66**	**5**	**33**	82	39	(2)	12
Total non-interest income	**1,420**	**1,382**	**1,246**	**1,469**	1,394	1,208	995	1,177
Operating and other expenses								
Salaries and related expenses	**1,339**	**1,338**	**1,215**	**1,282**	1,314	1,434	1,356	1,186
Building and equipment maintenance and depreciation	**452**	**443**	**489**	**449**	494	452	446	427
Amortization of intangible assets	**3**	**79**	**3**	**3**	8	4	5	6
Other expenses	**460**	**583**	**472**	**323**	795	404	393	376
Total operating and other expenses	**2,254**	**2,443**	**2,179**	**2,057**	2,611	2,294	2,200	1,995
Profit before taxes	**821**	**929**	**822**	**1,101**	181	494	386	785
Provision for taxes on profit	**299**	**345**	**284**	**463**	233	113	159	306
Profit (loss) after taxes	**522**	**584**	**538**	**638**	(52)	381	227	479
Banking corporation's share in profits of companies included on equity basis, after tax	**(165)**	**(17)**	**(54)**	**(57)**	(199)	108	63	(39)
Net profit (loss):								
Before attributiing to non-controlling interests	**357**	**567**	**484**	**581**	(251)	489	290	440
Attributed to non-controlling interests	**(9)**	**(12)**	**(10)**	**(11)**	(8)	(10)	(10)	(9)
Attributable to shareholders of the banking corporation	**348**	**555**	**474**	**570**	(259)	479	280	431
Basic and diluted earnings per share:								
Net profit (loss) attributable to shareholders of the banking corporation (in NIS)	**0.23**	**0.38**	**0.32**	**0.39**	(0.18)	0.33	0.19	0.29

Certification

I, Rakefet Russak-Aminoach, certify that:

1. I have reviewed the Annual Report of Bank Leumi le-Israel B.M. (the "Bank") for the year 2013 (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;

   (c) We have evaluated the effectiveness of the Bank's disclosure controls and procedures and presented our conclusions regarding 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 the fourth quarter that has materially affected, or is reasonably likely to materially affect, the Bank's internal control over financial reporting.

5. I and the Bank's other certifying officers have disclosed to the Joint Auditors, the Board of Directors and 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.

30 March 2014

Rakefet Russak-Aminoach
President and Chief Executive Officer

Certification

I, Ron Fainaro, certify that:

1. I have reviewed the Annual Report of Bank Leumi le-Israel B.M. (the "Bank") for the year 2013 (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;

   (c) We have evaluated the effectiveness of the Bank's disclosure controls and procedures and presented our conclusions regarding 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 the fourth quarter that has materially affected, or is reasonably likely to materially affect, the Bank's internal control over financial reporting.

5. I and the Bank's other certifying officers have disclosed to the Joint Auditors, the Board of Directors and 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.

30 March 2014

Ron Fainaro
Executive Vice President,
Head of Economics and Finance Division

Certification

I, Shlomo Goldfarb, certify that:

1. I have reviewed the Annual Report of Bank Leumi le-Israel B.M. (the "Bank") for the year 2013 (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;

   (c) We have evaluated the effectiveness of the Bank's disclosure controls and procedures and presented our conclusions regarding 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 the fourth quarter that has materially affected, or is reasonably likely to materially affect, the Bank's internal control over financial reporting.

5. I and the Bank's other certifying officers have disclosed to the Joint Auditors, the Board of Directors and 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.

30 March 2014

Shlomo Goldfarb
Executive Vice President
Chief Accounting Officer
Head of Accounting Division

Report of the Board of Directors and Management on Internal Control over Financial Reporting

The Board of Directors and Management of Bank Leumi le-Israel B.M. (henceforth: "the Bank"), are responsible for establishing and maintaining appropriate internal control over financial reporting (as defined in the Public Reporting Directives concerning "The Directors' Report"). The internal control system of the Bank has been designed to provide a reasonable level of confidence to the Board of Directors and Management of the Bank concerning the preparation and appropriate presentation of financial statements published in accordance with accepted accounting principles and the directives of the Supervisor of Banks and his instructions. Irrespective of the quality level of their design, all internal control systems have inherent limitations. Therefore even if it is determined that they are effective, they can only provide a reasonable level of confidence with reference to the preparing and presentation of a financial statement.

The Management, under the supervision of the Board of Directors, maintains a comprehensive internal control system designed to ensure that transactions are executed in accordance with the authorizations of Management, that assets are protected, and that accounting entries are reliable. Furthermore, Management, under the supervision of the Board of Directors, takes steps to ensure that channels of information and communication are effective and monitor performance, including performance of internal control procedures.

The Management of the Bank, under the supervision of the Board of Directors, has evaluated the effectiveness of internal control of the Bank over financial reporting as at 31 December 2013, based on the criteria determined in the internal control model of the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on this evaluation, the Management believes that as at 31 December 2013, the Bank's internal control over financial reporting is effective.

The effectiveness of the Bank's internal control over financial reporting as at 31 December 2013 was audited by the Bank's Auditors, Kost Forer Gabbay & Kasierer and Somekh Chaikin, as stated in their Report on page 290, which includes an unqualified opinion regarding the effectiveness of the Bank's internal control over financial reporting as at 31 December 2013.

30 March 2014

David Brodet
Chairman of the Board of Directors

Rakefet Russak-Aminoach
President and Chief Executive Officer

Ron Fainaro
Executive Vice President
Head of Economics and Finance Division

Shlomo Goldfarb
Executive Vice President
Chief Accounting Officer
Head of Accounting Division

Report of the Joint Auditors to the Shareholders of Bank Leumi le-Israel B.M. in accordance with Public Reporting Directives of the Supervisor of Banks regarding Internal Control over Financial Reporting

We have audited the internal control of Bank Leumi le-Israel B.M. and subsidiaries (hereinafter together: "the Bank") over financial reporting as of 31 December 2013, based on criteria established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Bank's Board of Directors and Management are responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Report of the Board of Directors and Management on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Bank's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (PCAOB) in the United States regarding the audit of internal control over financial reporting, as adopted by the Institute of Certified Public Accountants in Israel. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A bank's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles in Israel (Israeli GAAP) and with the directives and guidelines of the Supervisor of Banks. A bank's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and transfers of the assets of the company (including dispositions); (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles in Israel (Israeli GAAP), and the directives and guidelines of the Supervisor of Banks, and that receipt and payment of funds of the Bank are being made only in accordance with authorizations of the Management and Board of Directors of the Bank; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the Bank's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Bank maintained, in all material respects, effective internal control over financial reporting as at 31 December 2013, based on criteria established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

We have also audited, in accordance with generally accepted auditing standards in Israel, and certain auditing standards, of which implementation in audit of banking institutions was required in directives and guidelines of the Supervisor of Banks, the consolidated balance sheets of the Bank and its subsidiaries as at 31 December 2013 and 2012, the consolidated statements of profit an loss, the consolidated statements of comprehensive income, the consolidated statements of changes in equity, and the consolidated statements of cash flows for each of the three years ended 31 December 2013, and our report of 30 March 2014 included an unqualified opinion on those financial statements, as well as drawing attention to that stated in Notes 18.D paragraph 2, 18.I, paragraphs 1-3, and 18.K.

Kost Forer Gabbay & Kasierer
Certified Public Accountants (Isr.)

Somekh Chaikin
Certified Public Accountants (Isr.)

Joint Auditors

30 March 2014

Report of the Joint Auditors to the Shareholders of Bank Leumi le-Israel B.M.
Annual Financial Statements

We have audited the accompanying consolidated balance sheets of Bank Leumi le-Israel B.M. ("the Bank") and its consolidated companies ("the Group") as at 31 December 2013 and 2012, and the related consolidated statements of profit and loss, statements of changes in shareholders' equity and the consolidated statements of cash flows for each of the three years, the last of which ended 31 December 2013. These financial statements are the responsibility of the Bank's Board of Directors and of its Management. Our responsibility is to express an opinion on these financial statements based on our audits.

We did not audit the financial statements of the consolidated subsidiaries, whose assets constitute approximately 1.9% and 2.2% of the total consolidated assets as at 31 December 2013 and 2012, respectively, and whose net interest income before expenses for credit losses included in the consolidated statements of profit and loss constitutes about 0.7%, 0.7% and 1% of the total consolidated interest income before expenses for credit losses for the years ended 31 December 2013, 2012, and 2011, respectively. The financial statements of those subsidiaries were audited by other auditors whose reports thereon have been furnished to us and our opinion, insofar as it relates to amounts included in respect of these companies, is based on the reports of the other auditors.

We conducted our audits in accordance with generally accepted auditing standards in Israel, including standards prescribed by the Auditors (Manner of Auditor's Performance) Regulations, 1973 and certain auditing standards implementation of which in audit of banking institutions was required in directives and guidelines of the Supervisor of Banks. Such standards require that we plan and perform the audit to obtain reasonable assurance that the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the Board of Directors and by Management of the Bank, as well as evaluating the appropriateness of the overall financial statement presentation. We believe that our audits and the reports of other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the financial position of the Bank as at 31 December 2013 and 2012, and the results of operations, changes in shareholders' equity and cash flows of the Bank for each of the three years the last of which ended 31 December 2013, in conformity with generally accepted accounting principles (Israeli GAAP). Furthermore, the above financial statements have, in our opinion, been prepared in accordance with the directives and guidelines of the Supervisor of Banks.

Without qualifying our above opinion, we draw attention to:

1. that stated in Note 18.D paragraph 2, regarding claims against the Bank including petitions for their approval as class actions.
2. that stated in Note 18.I paragraphs 1-3, regarding matters concerning a company included on equity basis and its investee companies.
3. that stated in Note 18.K regarding investigations carried out against the Group in connection with its activity with US customers.

The Bank is unable to estimate the implications of the above-mentioned matters on the Bank, if any, on its financial position and operating results, and whether or not they will be material.

We have also audited, in accordance with the standards of the PCAOB (Public Company Accounting Oversight Board) in the United States regarding the audit of internal control over financial reporting, as adopted by the Institute of Certified Public Accountants in Israel, internal control over financial reporting of the Bank as of 31 December 2013, based on criteria established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and our report of 30 March, 2014 included an unqualified opinion on the effectiveness of internal control on financial reporting by the Bank.

Kost Forer Gabbay & Kasierer
Certified Public Accountants (Isr.)

Somekh Chaikin
Certified Public Accountants (Isr.)

Joint Auditors

30 March 2014

Bank Leumi le-Israel B.M. and its Consolidated Companies
Consolidated Balance Sheet as at 31 December 2013

	Note	31 December 2013	31 December 2012
		(NIS millions)	
Assets			
Cash and deposits with banks	2,14	44,351	54,621
Securities	3,14	63,735	56,408
Securities borrowed or purchased under agreements to resell		1,360	1,435
Credit to the public	4	244,757	245,378
Allowance for credit losses	4	(3,883)	(4,114)
Credit to the public, net		240,874	241,264
Credit to governments	5	558	442
Investments in companies included on equity basis	6	1,689	2,129
Buildings and equipment	7	3,638	3,705
Intangible assets and goodwill	6E	99	189
Assets in respect of derivative instruments	18B	13,054	11,438
Other assets	8	5,002	4,529
Total assets		374,360	376,160
Liabilities and equity			
Deposits of the public	9	286,003	289,538
Deposits from banks	10	4,310	4,073
Deposits from governments		397	451
Securities lent or sold under agreements to repurchase		624	1,007
Debentures, bonds and subordinated notes	11	25,441	27,525
Liabilities in respect of derivative instruments	18B	13,487	12,762
Other liabilities	12	17,333	15,576
Total liabilities		347,595	350,932
Non-controlling interests		340	307
Equity attributable to shareholders of the banking corporation		26,425	24,921
Total equity	13	26,765	25,228
Total liabilities and equity		374,360	376,160

The accompanying notes are an integral part of these condensed financial statements.
For the condensed financial statements of the Bank only – see Note 30.

David Brodet
Chairman of the Board of Directors

Prof. Efraim Sadka
Director

Zipporah Samet
Director

Rakefet Russak-Aminoach
President and Chief Executive Officer

Ron Fainaro
Executive Vice President,
Head of Economics and Finance Division

Shlomo Goldfarb
Executive Vice President,
Chief Accounting Officer,
Head of Accounting Division

Date of approval of the financial statements: 30 March 2014

Bank Leumi le-Israel B.M. and its Consolidated Companies
Consolidated Statement of Profit and Loss
for the year ended 31 December 2013

		2013	2012	2011
	Note	(NIS millions)		
Interest income	**20**	**12,134**	13,507	14,283
Interest expenses	**20**	**4,777**	6,099	7,176
Interest income, net	**20**	**7,357**	7,408	7,107
Expenses in respect of credit losses	**4**	**268**	1,236	734
Net interest income after expenses in respect of credit losses		**7,089**	6,172	6,373
Non-interest income				
Non-interest financing income	**21**	**1,127**	444	11
Commissions	**22**	**4,188**	4,199	4,116
Other income	**23**	**202**	131	48
Total non-interest income		**5,517**	4,774	4,175
Operating and other expenses				
Salaries and related expenses	**24**	**5,174**	5,290	5,061
Building and equipment maintenance and depreciation	**7**	**1,833**	1,819	1,704
Amortization of intangible assets	**6e**	**88**	23	2
Other expenses	**25**	**1,838**	1,968	1,574
Total operating and other expenses		**8,933**	9,100	8,341
Profit before taxes		**3,673**	1,846	2,207
Provision for taxes on profit	**26**	**1,391**	811	418
Profit after taxes		**2,282**	1,035	1,789
Share of the banking corporation share in profits (losses) of companies included on equity basis, after tax	**6**	**(293)**	(67)	148
Net profit:				
Before attributing to non-controlling interests		**1,989**	968	1,937
Attributed to non-controlling interests		**(42)**	(37)	(46)
Attibuted to shareholders of the banking corporation		**1,947**	931	1,891
Earnings per share				
Basic and diluted earnings per share:				
Net profit attibuted to shareholders of the banking corporation (in NIS)		**1.32**	0.63	1.28
Weighted average of the number of shares for calculation (in thousands of shares)		**1,473,551**	1,473,551	1,473,551

The accompanying notes are an integral part of the consolidated financial statements.
For condensed financial statements of the Bank only – see Note 30.

Bank Leumi le-Israel B.M. and its Consolidated Companies
Consolidated Statement of Comprehensive Income
for the year ended 31 December 2013

	2013	2012 (1)	2011 (1)
	(NIS millions)		
Net profit before attribution to non-controlling interests	**1,989**	968	1,937
Less net profit attributed to non-controlling interests	**42**	37	46
Net profit attributed to shareholders of the Bank	**1,947**	931	1,891
Other comprehensive income (loss), before taxes:			
Adjustments for showing securities available for sale at fair value, net	**(518)**	1,067	(1,023)
Adjustments for translation of financial statements, net (2), after the effect of tax and hedges (3)	**(115)**	(55)	381
Share of the banking corporation in other comprehensive loss of companies included on equity basis	**11**	-	73
Other comprehensive income (loss), before taxes	**(622)**	1,012	(569)
Relevant tax effect	**130**	(355)	336
Other comprehensive income (loss) before attribution to non-controlling interests, after taxes	**(492)**	657	(233)
Less other comprehensive loss attributed to non-controlling interests	**(3)**	-	(1)
Other comprehensive income (loss) attributed to shareholders of the banking corporation, after taxes	**(489)**	657	(232)
Comprehensive income before attribution to non-controlling interests	**1,497**	1,625	1,704
Comprehensive income attributed to non-controlling interests	**39**	37	45
Comprehensive income attributed to shareholders of the Bank	**1,458**	1,588	1,659

(1) On 1 January 2013, the Bank adopted for the first time the directives of the Supervisor of Banks on the statement of comprehensive income. Adoption of the directive was made on a retroactive basis. See Note 1 and Note 29.

(2) Adjustments for translation of financial statements of foreign operations whose functional currency differs from the functional currency of the Bank.

(3) Hedges – profits (losses) net in respect of hedging a net investment in foreign currency.

The accompanying notes are an integral part of these condensed consolidated interim financial statements.

Bank Leumi le-Israel B.M. and its Consolidated Companies
Statement of Changes in Shareholders' Equity
for the year ended 31 December 2013

		Capital reserves								
	Share capital	Premium	Share-based payment transactions and others (1)	Total share capital and capital reserves	Accumulated other comprehensive profit (loss)	Retained earnings (5)	Loans to employees for purchase of the Bank's shares	Total	Non-controlling interests	Total capital
	(NIS millions)									
Balance as at 1 January 2011	7,059	1,129	10	8,198	33	15,063	(1)	23,293	318	23,611
Adjustment of opening balances in respect of first time implementation of impaired debts and International Financial Reporting Standards (IFRS) (2) (3)	-	-	-	-	-	(1,090)	-	(1,090)	(14)	(1,104)
Net profit for the accounting year	-	-	-	-	-	1,891	-	1,891	46	1,937
Dividend paid	-	-	-	-	-	(400)	-	(400)	(15)	(415)
Employee benefit from share-based payment transactions	-	-	13	13	-	-	-	13	-	13
Adjustments in respect of companies included on equity basis, net	-	-	-	-	-	(11)	-	(11)	-	(11)
Other comprehensive loss, net after the effect of tax (4)	-	-	-	-	(232)	-	-	(232)	(1)	(233)
Changes in non-controlling interests	-	-	-	-	-	(47)	-	(47)	(80)	(127)
Loans to employees for purchase of the Bank's shares	-	-	-	-	-	-	(43)	(43)	-	(43)
Balance as at 31 December 2011	7,059	1,129	23	8,211	(199)	15,406	(44)	23,374	254	23,628
Adjustment of opening balances in respect of first time implementation of International Financial Reporting Standards (IFRS) (2)	-	-	-	-	-	(26)	-	(26)	-	(26)
Net profit for the period	-	-	-	-	-	931	-	931	37	968
Dividend paid by consolidated companies	-	-	-	-	-	-	-	-	(8)	(8)
Adjustments in respect of companies included on equity basis, net	-	-	-	-	-	(9)	-	(9)	-	(9)
Other comprehensive loss, net after the effect of tax (4)	-	-	-	-	657	-	-	657	-	657
Changes in non-controlling interests	-	-	-	-	-	(6)	-	(6)	24	18
Balance as at 31 December 2012	7,059	1,129	23	8,211	458	16,296	(44)	24,921	307	25,228
Net profit for the period	-	-	-	-	-	1,947	-	1,947	42	1,989
Dividend paid by consolidated companies	-	-	-	-	-	-	-	-	(6)	(6)
Adjustments in respect of companies included on equity basis, net	-	-	-	-	-	24	-	24	-	24
Employee benefit from share-based payment transactions	-	-	10	10	-	-	-	10	-	10
Other comprehensive loss, net after the effect of tax (4)	-	-	-	-	(489)	-	-	(489)	(3)	(492)
Changes in non-controlling interests	-	-	-	-	-	11	-	11	-	11
Loans to employees for purchase of the Bank's shares	-	-	-	-	-	-	1	1	-	1
Balance as at 31 December 2013	7,059	1,129	33	8,221	(31)	18,278	(43)	26,425	340	26,765

See notes on next page.

Bank Leumi le-Israel B.M. and its Consolidated Companies
Statement of Changes in Shareholders' Equity
for the year ended 31 December 2013 (cont'd)

(1) Including NIS 10 million other capital reserves.

(2) In 2012 in respect of implementation of IAS 12, an amount of NIS 42 million; in 2011, adjustments from translation of financial statements of investee companies overseas whose functional currency differs from the functional currency of the Bank were transferred to accumulated retained earnings following the change to reporting under IAS 21 in the amount of NIS 381 million.

(3) Including NIS 721 million in respect of the change to implementation of the Impaired Debts Directives (NIS 1,319 million gross).

(4) On 1 January 2013, the Bank implemented for the first time the directives of the Supervisor of Banks on the statement of comprehensive income. Comparative figures were reclassified to adapt to the new manner of presentation. See also Note 1.

(5) Including NIS 471 million not available for distribution as a dividend (31 December 2012 – NIS 208 million, 31 December 2011 – NIS 379 million). The balance of the amount for allocation is subject to Bank of Israel directives and the limitations set out in Proper Conduct of Banking Business Directives.

The accompanying notes are an integral part of the consolidated financial statements.

Bank Leumi le-Israel B.M. and its Consolidated Companies
Consolidated Statement of Cash Flows
for the year ended 31 December 2013

	2013	2012	2011 (1)
	(NIS millions)		
Cash flows from operating activities			
Net profit for the year	**1,989**	968	1,937
Adjustments:			
Group share in undistributed losses (profits) of companies included on equity basis (2)	**335**	181	(72)
Expenses deriving from share-based payment transactions	**10**	-	13
Depreciation of buildings and equipment (including impairment)	**768**	775	707
Amortization	**88**	23	2
Expenses in respect of credit losses	**268**	1,236	734
Provision for impairment of assets transferred to group ownership	**1**	9	11
Net profit on sale of available-for-sale securities (including impairment)	**(747)**	(201)	(39)
Realized and unrealized profit from adjustment to fair value of securities held for trading	**(35)**	(239)	(313)
Loss (gain) on realization of investments in companies included on equity basis after tax	**(15)**	(24)	4
Loss (gain) on sale of buildings and equipment	**(25)**	(2)	2
Interest received (and not yet received) in respect of debentures available for sale	**(140)**	(100)	(822)
Unpaid interest in respect of debentures and subordinated notes	**1,428**	356	602
Effect of exchange rate differentials on cash and cash equivalents	**653**	131	(607)
Deferred taxes, net	**(127)**	(635)	(308)
Increase in excess of provisions for severance pay and pensions over amounts funded	**132**	568	620
Other, net	**(2)**	(2)	8
Net change in current assets:			
Deposits with banks for an original period of over 3 months	**1,112**	333	(1,956)
Credit to the public	**(893)**	(1,822)	(19,226)
Credit to governments	**(118)**	7	(69)
Securities borrowed or purchased under agreements to resell	**75**	(210)	(35)
Assets in respect of derivative instruments	**(1,595)**	135	(2,848)
Securities held for trading	**652**	(734)	(754)
Other assets	**279**	(31)	(481)
Net change in current liabilities:			
Deposits from banks	**283**	(984)	2,602
Deposits of the public	**(1,986)**	10,459	27,055
Deposits from the government	**(38)**	(62)	(141)
Securities lent or sold under agreements to repurchase	**(381)**	566	(564)
Liabilities in respect of derivative instruments	**856**	657	1,923
Other liabilities	**1,158**	92	670
Net cash from operating activities	**3,985**	11,450	8,655

See notes on next page.
The accompanying notes are an integral part of the consolidated financial statements.
For condensed financial statements of the Bank only, see Note 30.

Bank Leumi le-Israel B.M. and its Consolidated Companies
Consolidated Statement of Cash Flows (cont'd)
for the year ended 31 December 2013

	2013	2012	2011 (1)
	(NIS millions)		
Cash flows from investment activities			
Acquisition of available-for-sale securities	**(61,350)**	(50,487)	(26,345)
Proceeds from sale of available-for-sale securities	**33,528**	25,727	28,907
Proceeds from redemption from available-for-sale securities	**19,785**	18,911	6,782
Acquisition of subsidiary consolidated for the first time (Appendix A)	**-**	-	1,848
Acquisition of shares in companies included on equity basis	**(66)**	(66)	(110)
Proceeds from realization of investment in companies included on equity basis	**73**	64	50
Repayment of shareholders' loan to company included on equity basis	**4**	4	2
Acquisition of buildings and equipment	**(698)**	(770)	(755)
Proceeds from realization of buildings and equipment	**39**	9	6
Proceeds from realization of assets transferred to group ownership	**3**	14	7
Net cash from investment activities	**(8,682)**	(6,594)	10,392
Cash flows from financing activities			
Issue of debentures and subordinated notes	**-**	2,420	3,386
Redemption of debentures and subordinated notes	**(3,512)**	(5,250)	(928)
Issue of capital in consolidated companies to minority shareholders	**-**	21	-
Additional purchase of shares in consolidated companies	**-**	-	(115)
Dividend paid to shareholders	**-**	-	(900)
Dividend paid to minority shareholders in consolidated companies	**(6)**	(8)	(15)
Loans to employees for purchase of the Bank's shares	**1**	-	(43)
Net cash from financing activities	**(3,517)**	(2,817)	1,385
Increase (decrease) in cash and cash equivalents	**(8,214)**	2,039	20,432
Balance of cash and cash equivalents at beginning of year	**51,644**	49,736	28,697
Effect of exchange rate fluctuations on balances of cash and cash equivalents	**(653)**	(131)	607
Balance of cash and cash equivalents at end of year	**42,777**	51,644	49,736

(1) Comparative figures have been reclassified in order to adapt to the current method of presentation.
(2) Less dividend received.

The accompanying notes are an integral part of the consolidated financial statements.
For condensed financial statements of the Bank only, see Note 30.

Bank Leumi le-Israel B.M. and its Consolidated Companies
Consolidated Statement of Cash Flows (cont'd)
for the year ended 31 December 2013

Interest and taxes paid and/or received and dividends received

	2013	2012	2011
	(NIS millions)		
Interest received	**12,474**	13,823	14,027 (1)
Interest paid	**(5,360)**	(7,077) (1)	(7,222) (1)
Dividends received	**69**	170	153
Taxes paid on income	**(1,238)**	(1,113)	(963)

(1) Restated.

Appendix A - Net cash flow from acquisition of a subsidiary consolidated for the first time:

	2011
	(NIS millions)
Assets and liabilities of a subsidiary that was consolidated and cash flow from acquisition of subsidiary that was consolidated, as at date of acquisition:	
Cash and cash equivalents acquired	2,426
Assets (excluding cash and cash equivalents)	635
Liabilities	(2,621)
Identifiable assets and liabilities	440
Goodwill and intangible assets	138
Total cost of acquisition	578
Less non-cash proceeds for acquisition of consolidated subsidiary	-
Proceeds paid in cash	(578)
Less cash and cash equivalents acquired	2,426
Cash flow from acquisition of subsidiary consolidated for the first time	1,848

The accompanying notes are an integral part of the consolidated financial statements.
For condensed financial statements of the Bank only, see Note 30.

Appendix B – Non-cash investment and financing transactions in the reporting period:

In 2013:

(1) During the year, assets were transferred from credit to the public to other assets, in the amount of NIS 2 million, in respect of loans that were repaid.

(2) During the year, fixed assets were acquired against liabilities to suppliers, in the amount of NIS 24 million.

In 2012:

(1) During the year, fixed assets were acquired against liabilities to suppliers, in the amount of NIS 66 million.

The accompanying notes are an integral part of the consolidated financial statements.
For condensed financial statements of the Bank only, see Note 30.

Index to Notes

Note 1 – Significant Accounting Policies

A. General

The financial statements have been prepared in accordance with generally accepted accounting principles in Israel (Israeli GAAP) and the directives and guidelines of the Supervisor of Banks relating to the preparation of annual financial statements of a banking corporation.

Publication of the financial statements is on the basis of the consolidated statements only. Condensed financial statements of the Bank on a single-entity basis appear in Note 29.

The financial statements were approved for publication by the Board of Directors of the Bank on 30 March 2014.

B. Definitions

In these financial statements -

The Group – the banking corporation and its subsidiaries.

Consolidated companies - companies of which the financial statements are fully consolidated, directly or indirectly, in the statements of the Bank.

Companies included on equity basis - companies, other than consolidated companies, and companies consolidated under proportional consolidation including a partnership or joint enterprise, in which the Bank's investment is included, directly or indirectly, in the financial statements on equity basis.

Investee companies - consolidated companies, companies consolidated under proportional consolidation, or companies included on equity basis.

Overseas units - representative offices, agencies, branches or consolidated companies of the Bank outside Israel.

Functional currency - the currency of the main economic environment in which the Bank generally operates. This is the currency of the environment where the corporation produces and spends most of its cash funds.

Reporting currency - the currency in which the financial statements are reported.

Related parties - as defined in IAS 24 – Related Party Disclosures, except for interested parties.

Interested parties - as defined in paragraph 1 of the Securities Law, 1968.

Index - the Consumer Price Index in Israel published by the Central Bureau of Statistics.

Adjusted amount - historical nominal amount adjusted to the December 2003 CPI, in accordance with the provisions of Opinions 23 and 36 of the Institute of Certified Public Accountants in Israel.

Reported amount - amount adjusted to the transition date (31 December 2003) with the addition of amounts in nominal values that were added after the transition date and less amounts that were eliminated after the transition date.

Nominal financial reporting - financial reporting based on reported amounts.

Adjusted financial reporting - financial reporting in values adjusted according to the changes in the general purchasing power of the Israeli currency in accordance with the provisions of the opinions of the Institute of Certified Public Accountants in Israel.

Cost – cost in reported amount.

Fair value - the amount that would be received from the sale of an asset or that would be paid to transfer a liability in a transaction between a willing seller and a willing buyer at the measurement date.

Recorded debt balance – the recorded debt balance is defined as the outstanding debt after deducting accounting write-offs, but before deducting an allowance for credit losses in respect of that debt.

C. Basis for preparation of the financial statements

1. Reporting principles

The financial statements of the Bank have been prepared in accordance with generally accepted accounting principles in Israel (Israeli GAAP) and the directives and guidelines of the Supervisor of Banks. In preparing the financial statements, the Bank implements, *inter alia*, certain International Financial Reporting Standards (IFRS) and accounting principles generally accepted by US banks, in the manner explained below:

- On subjects that are a core part of the banking business – the accounting treatment is in accordance with the Public Reporting Directives and instructions of the Supervisor of Banks and in accordance with accounting principles generally accepted by US banks that were adopted within the framework of the Public Reporting Directives of the Supervisor of Banks.

- On subjects that are not a core part of the banking business – the accounting treatment is in accordance with accounting principles generally accepted in Israel and in accordance with International Financial Reporting Standards (IFRS) and interpretations of the International Financial Reporting Interpretations Committee (IFRIC), as set out in the directives and instructions of the Supervisor of Banks. International standards are implemented in accordance with the principles detailed below:

  1.1 In cases where a material issue arises that is not addressed in the international standards or the Supervisor's instructions for implementation, the Group treats the issue in accordance with accounting principles generally accepted by US banks that apply specifically to these issues;

  1.2 In cases where there is no specific reference in the standards or interpretations to material issues, or there are a number of alternatives for the treatment of a material issue, the group acts according to specific implementation instructions decided on by the Supervisor;

  1.3 In those places where an international standard that has been adopted contains a reference to another international standard adopted in the Public Reporting Directives, the Group acts in accordance with the provisions of the International Standard;

  1.4 In those places where an international standard that has been adopted contains a reference to another international standard not adopted in the Public Reporting Directives, the Group acts in accordance with the Reporting Directives and with accounting principles generally accepted in Israel;

Note 1 – Significant Accounting Policies (cont'd)

1.5 In those places where an international standard that has been adopted contains a reference to a definition of a term defined in the Public Reporting Directives, the reference to the definition in the Directives shall replace the original reference.

For details of the International Financial Reporting Standards implemented for the first time, see paragraph D below.

2. Functional currency and reporting currency

The financial statements are reported in new shekels rounded to the nearest million, unless stated otherwise.

The shekel is the currency representing the principal economic environment in which the Bank operates.

For information on the functional currency of banking units operating overseas, see Note E below.

3. Basis of measurement

3.1 General

The financial statements are shown in reported amounts in accordance with the accounting standards of the Israeli Accounting Standards Board and the directives of the Supervisor of Banks.

Amounts of non-monetary assets do not necessarily show realizable value or current economic value, but only the amounts reported for those assets.

3.2 Balance Sheet

- Non-monetary items (mainly buildings and equipment; investments in non-quoted shares; amortizable expenses relating to issuance of debentures, bonds and subordinated notes) and share capital are shown in reported amounts.

- Monetary items are shown in the balance sheet at historical nominal values as at the balance sheet date, except for derivative financial instruments and other financial instruments that are measured at fair value.

- The equity value of investments in companies included on equity basis is determined based on the financial statements of these companies in reported amounts or translated to new Israeli shekels.

3.3 Profit and Loss Statement

- Income and expenses that arise from non-monetary items (for example, depreciation and amortization and prepaid income and expenses) or from provisions included in the balance sheet are derived from the difference between the reported amount of the opening balance and the reported amount of the closing balance.

- The Bank’s share in the operating results of investee companies and the share of external shareholders in the results of consolidated companies is determined based on the financial statements in reported amounts of these companies.

- Other components of the profit and loss statement are shown at their nominal values (for example, net interest income, commissions).

3.4 Statement of changes in shareholders' equity

Dividend declared or paid in the year of the report is stated in nominal values.

4. Use of estimates

When preparing the financial statements, in accordance with generally accepted accounting principles in Israel and directives and guidelines of the Supervisor of Banks, management is required to use estimates, evaluations and their discretion affecting the reported amounts of assets and liabilities, the disclosure relating to contingent assets and liabilities and amounts of income and expenses during the reporting period. It should be made clear that actual results may differ from such estimates.

When formulating accounting estimates used in preparing the Bank's financial statements, Bank management has to make assumptions concerning circumstances and events which involve significant uncertainty. In its consideration of the estimates, Bank management bases itself on past experience, various facts, external factors, and on reasonable assumptions in accordance with circumstances appropriate to each estimate.

Changes in estimates

The estimates and the assumptions on which they are based are reviewed on a routine basis. Changes in accounting estimates are recognized in the period in which the estimates were amended and for each period affected in the future.

D. First-time Implementation of Accounting Standards, Updates to Accounting Standards, and Directives of the Banking Supervision Department

As of reporting periods commencing 1 January 2013, the Bank implements the accounting standards and directives set out below:

1. Directive on "Statement of Comprehensive Income".

2. New system of International Financial Reporting Standards (IFRS) on consolidating financial statements and related issues.

3. Directive on "Offsetting Assets and Liabilities".

4. Directive on "Disclosure of Deposits".

5. Directive on updating the disclosure of credit quality of debts and the allowance for credit losses, adopting Accounting Standard Update ASU 2010-20.

6. Letter of the Supervisor of Banks on "Updated Instructions on Residential Property" .

7. Updates to the Note on securities set out in the Supervisor's circular on integrating Banking Supervision Department letters in the Reporting Directives.

8. Updates in connection with the presentation of the Note on assets and liabilities by linkage basis and repayment periods.

The effect of implementation of these Standards is shown below as part of the Accounting Policy.

Reclassification

Directive on statement of comprehensive income

Pursuant to the first-time implementation of the directives of the Banking Supervision Department on adapting the manner of presentation of the statement of comprehensive income to the requirements of generally accepted accounting principles in the U.S. (ASU 2011-05, ASU 2011-12), items of other comprehensive income in the financial statements for 2012 and 2011 have been reclassified and are not separately in the Statement of Changes in Shareholders' Equity, but are reported in total with details of the composition reported in a separate report called "Consolidated Statement of Comprehensive Income" shown immediately after the Statement of Profit and Loss.

E. Foreign currency and linkage

Transactions in foreign currency

Assets and liabilities denominated in foreign currency or linked thereto are stated according to the representative rates of exchange published by Bank of Israel at the balance sheet date, or other appropriate date, as follows:

- Assets and liabilities denominated in foreign currency or linked thereto are translated to the functional currency at the rate of exchange prevailing on that date.

- Non-monetary assets and liabilities in foreign currency or linked thereto that are measured at fair value, are translated into the functional currency at the rate of exchange prevailing on the date on which the fair value is determined. Non-monetary items denominated in foreign currency or linked thereto and measured at historical cost, are translated at the rate of exchange prevailing on the date of the transaction.

Income and expenses in foreign currency are included in the statement of profit and loss according to current representative exchange rates at the transaction dates with the addition of exchange rate differentials on the assets and liabilities in respect of which the above income and expenses arose.

Exchange rate differentials resulting from translation to the functional currency are recognized in profit and loss except for the following differences recognized in other comprehensive income resulting from the translation of:

- Equity financial instruments classified as available for sale (except in the event of impairment when the translation differences recognized in other comprehensive income are reclassified to profit and loss).

- Financial liabilities hedging investments in a foreign operation in respect of the effective part of the hedge.

- Cash flow hedge in respect of the effective part of the hedge.

The functional currency of offices operating overseas

The Bank applies IAS 21 – "The Effects of Changes in Foreign Exchange Rates" as of 1 January 2011, except for the provisions of the Standard with regard to the classification of banking offices operating overseas as foreign operations whose functional currency is not the shekel.
Until 1994 certain foreign banking offices were considered as a foreign operation whose functional currency is different from the shekel, and exchange rate differentials were charged directly to equity, as

part of the translation reserve. From 1995, pursuant to the directives of the Supervisor of Banks, foreign banking offices were classified as a foreign operation whose functional currency is the same as the functional currency of the Bank.

On 14 February 2012, instructions were published by the Supervisor of Banks as to the manner of determining the functional currency of banking offices operating overseas. When determining the functional currency, the Bank is required to examine the range of criteria listed below, and document the results:

- If the primary environment in which the office generates and expends cash is a foreign currency and the activity of the office in shekels is marginal.

- If recruiting customers for the office is carried out independently, such that the activity of the office vis-à-vis the customers of the banking corporation or related parties is not significant.

- If the activity of the office vis-à-vis the banking corporation and related parties is not significant, and, *inter alia*, the office has no dependence on sources of funding from the banking corporation or its related parties.

- If the activity of the office is essentially independent and stands alone, and is not an extension of or supplementary to the local activity of the banking corporation.

When one of the said criteria is clearly not fulfilled (for example, the transactions of the office carried out with the banking corporation's customers are so significant that they represent most of the office's transactions), this indicates that the office is to be treated as a foreign operation whose functional currency is the shekel. In any other situation, the determination is to be made according to an examination of a range of criteria.

The Bank has reexamined the classification of its overseas banking offices in accordance with the new criteria, and has reclassified the banking offices in the US and Switzerland as foreign operations whose functional currency is other than the shekel.
The change in classification was dealt with prospectively as a change in the functional currency of the offices, so that exchange rate differences from translation are recognized from 1 January 2012 as other comprehensive income, and shown under "Adjustments for translation of foreign operations".

Foreign operation

The assets and liabilities of foreign operations, including goodwill and fair value adjustments generated in an acquisition, have been translated to NIS at the exchange rate prevailing at the date of the transactions.
Exchange rate differentials in respect of the translation are recognized in comprehensive income, and are shown in equity under "Adjustments for translation of financial statements".
On realization of a foreign operation leading to loss of control or substantial influence, the cumulative amount in the translation reserve resulting from the foreign operation is reclassified to profit and loss as part of the profit or loss on the realization.

Hedging a net investment in a foreign operation

The Group applies hedge accounting in respect of exchange rate differences between the functional currency of a foreign operation and the functional currency of the Bank (NIS), whether the investment in a foreign operation is held directly by the Bank or through a holding company.
Exchange rate differences arising from translation of a financial liability hedging a net investment in a foreign operation, are charged to other comprehensive income and shown as equity under "Adjustments for translation of foreign operations". The ineffective part is charged to profit and loss. When the investment for which the hedging was made is realized, the relevant amount accrued

in "Adjustments for translation of financial statements" is transferred to profit and loss as part of the profit and loss from realization of the investment.

Index-linked assets and liabilities not measured at fair value

Assets and liabilities linked to the Consumer Price Index are included in accordance with the linkage terms determined for each balance.

Details of representative exchange rates and the CPI and the rate of change therein:

	31 December			Rate of change in		
	2013	2012	2011	**2013**	2012	2011
	NIS			%		
Exchange rate of:						
U.S. dollar	**3.471**	3.733	3.821	**(7.0)**	(2.3)	7.7
Euro	**4.782**	4.921	4.938	**(2.8)**	(0.3)	4.2
Pound Sterling	**5.742**	6.037	5.892	**(4.9)**	2.5	7.3
Swiss franc	**3.897**	4.077	4.062	**(4.4)**	0.4	7.2
Consumer Price Index:	(Points)					
November – known index	**107.5**	105.5	104.0	**1.9**	1.4	2.6
December – index for the month	**107.6**	105.7	104.0	**1.8**	1.6	2.2

F. Basis of consolidation

1. Business combinations

The Group applies the acquisition method with regard to all business combinations. The acquisition date is the date when the acquirer achieved control over the acquiree. The Group controls the acquiree when it is exposed, or has rights, to varying returns from its involvement in the acquiree, and it has the ability to influence these returns.

The Group recognizes goodwill at the acquisition date at the fair value of the proceeds paid, including amounts recognized in respect of any rights not conferring control over an acquiree, as well as the fair value at the acquisition date of equity rights in the acquiree that were held prior to then by the acquirer, after deducting the net amount attributable on acquisition to identifiable assets that were acquired and liabilities that were assumed.

The Bank recognizes a contingent liability assumed in a business combination at the date of acquisition if there is a liability at the date of acquisition deriving from past events whose fair value can be measured in a reliable manner.

In the event the Group carries out an acquisition at an advantageous price (an acquisition that includes negative goodwill), it recognizes the profit generated as a result in the profit and loss statement at the acquisition date, after carrying out an additional examination of the amounts attributed to the assets and liabilities of the entity acquired.

The proceeds transferred include the fair value of the assets transferred to the previous owners of the acquiree, liabilities assumed by the acquirer vis-à-vis the previous owners of the acquiree, and equity rights issued by the Group. In a business combination achieved in stages, the difference between the fair value at the date of acquisition of the equity rights in the acquiree held previously by the Group, and the book value at the same date, is charged to the statement of profit and loss under "Non-interest financing income – profits or losses from investment in shares" as part of activities not for trading purposes. Furthermore, the proceeds transferred include the fair value of the conditional proceeds. Subsequent to the date of acquisition, the Group recognizes changes in the fair value of the conditional proceeds classified as a financial liability in the statement of profit and loss, while the conditional proceeds classified as a capital instrument is not remeasured.

Costs of a transaction resulting from a business combination transaction are charged immediately to profit and loss.

Business combinations occurring prior to 1 January 2011

Pursuant to the instructions of the Supervisor of Banks, the Group adopted the relief provided in IFRS 1 – First-time Implementation of International Financial Reporting Standards. Accordingly, the Group does not implement IFRS 3 (2008) retroactively with regard to business combinations, acquisitions of companies included on equity basis, and acquisitions of non-controlling interests occurring prior to 1 January 2011. Thus, for the said acquisitions, goodwill recognized and surplus costs generated represent the amounts recognized in accordance with the Public Reporting Directives of the Supervisor of Banks.

2. Subsidiary companies

Subsidiary companies are entities controlled by the Bank. Control exists when the Bank has the ability to determine the financial and operating policy of the entity in order to obtain benefit from its resources and activities. Control exists when the Bank holds, directly or indirectly, shares granting more than 50% of the voting rights and potential voting rights in the subsidiary and the rights to appoint the majority of the members of its Board of Directors, unless there are reasons which clearly prevent the parent company from implementing actual control.

The consolidated financial statements include the financial statements of the Bank and of entities in which the Bank has control. The financial statements of subsidiary companies are included in the consolidated financial statements from the date control is obtained until the date control ceases. The accounting policy of subsidiary companies was amended as necessary in order to adapt it to the accounting policy adopted by the Bank, except in those cases when the Supervisor of Banks otherwise permitted.

Intercompany balances and transactions between consolidated companies are eliminated in the consolidated financial statements.

The financial statements of two wholly-owned real estate and service companies are consolidated in the financial statements of the Bank only.

Non-controlling interests

Non-controlling interests are the part of the equity of subsidiary companies, directly or indirectly, which are not attributable to the parent company. These rights, which grant the holder part of the net assets of the acquiree, are measured for fair value on the date of acquisition.

Profit or loss and any element of other comprehensive income are attributable to the shareholders of the Bank and to non-controlling interests. The amount of profit, loss, and other comprehensive income attributable to the owners of the Bank and to non-controlling interest even if as a result of this the balance of non-controlling interests would be negative.

Transactions with non-controlling interests, while maintaining control, are treated as equity transactions. Any difference between the proceeds paid or received in the change of non-controlling interests is charged to the owners' share of the Bank, directly to retained earnings.

The amount for which non-controlling interests are adjusted is calculated as follows:

- If the holding percentage increases, according to the relative part acquired from the balance of the non-controlling interests in the consolidated financial statements prior to the transaction.

- If the holding percentage decreases, it is calculated according to the relative part realized by the owners of the bank in net assets of the subsidiary company including goodwill. Furthermore, when there are changes in the holding percentage in a subsidiary company, while maintaining control, the Bank reapportions the aggregate amounts recognized under other comprehensive income, between the owners and the non-controlling interests.

3. Companies included on equity basis

Companies included on equity basis are entities in which the Group has significant influence on financial and operational policy, without having achieved control over them. It is assumed that holding between 20% and 50% of an investee grants material influence. When examining whether there is material influence, potential voting rights that are exercisable or immediately convertible to shares in the investee company, are to be taken into consideration.

The investment in shares of companies included on equity basis is dealt with according to the equity method and recognized initially at cost. The cost of the investment includes transaction costs. When the Bank achieves significant influence for the first time in an investment dealt with as an asset available for sale until the date significant influence is achieved, the equity method is applied retroactively.

Investments include goodwill calculated at the date of acquisition and shown after deducting accrued losses from impairment. The accounting policy of companies included on equity basis which is implemented by them is in accordance with generally accepted accounting principles in Israel or international accounting principles if the company included on equity basis is in a foreign country or is otherwise permitted by the Supervisor of Banks.

The financial statements of a company included on equity basis are prepared using an uniform accounting policy with the banking corporation with regard to similar transactions and events under similar circumstances; except for adjustments to accounting policy referring to subjects that are a core part of the banking business, that were implemented by a non-banking company included on equity basis. In addition, the financial statements of companies included on equity basis are prepared for the same dates and periods as those of the banking corporation.

The Bank’s share in the operating results of the said companies is shown after amortization of the cost generated on their acquisition. Excess cost attributed to the assets and liabilities is amortized over the useful life of the asset. Positive goodwill is not amortized and is included in the book value of the investment, and negative goodwill is recognized in profit and loss at the acquisition date with the approval of the Supervisor of Banks.

The statement of changes in shareholders' equity includes the Bank's share in "translation adjustments" of units held by companies included on equity basis, as units whose activity is in a functional currency differing from the functional currency of the Bank.

Profits or losses from the realization of companies included on equity basis are charged to profit and loss under "Non-interest financing income – profits or losses from investment in shares" as part of activities not for trading purposes.
When the Group share in losses exceeds the value of the rights of the Group in the company dealt with under the equity method, the book value of those rights is reduced to zero.

The Group does not recognize additional losses of the investee company unless the Group has an additional obligation to the investee company. When there is an increase in the percentage of the holding in the company included on equity basis that is being dealt with under the equity method while retaining significant influence, the acquisition method is applied only with respect to the additional percentages held, while the previous holding remains unchanged.

When there is a reduction in the percentage of the holding in the company included on equity basis that is being dealt with under the equity method while retaining significant influence, the relative portion of the amounts recognized in capital reserves through other comprehensive profit in reference to the said company included on equity basis, is reclassified to profit and loss or retained earnings.

When there is a loss of significant influence, the Group ceases to use the equity method as of the date it lost significant influence, and deals with the remaining investment as a financial asset. At this date it will recognize, in profit and loss under "Non-interest financing income – profits or losses from investment in shares" as part of activities not for trading purposes, the difference between the fair value of the balance of the investment and the book value of the investment. The cost of rights sold for purpose of calculating the profit or the loss on the sale is determined by a weighted average.

In addition, at the same date a relative part of the amounts recognized in capital reserves by way of other comprehensive income, with reference to that company included on equity basis, is reclassified to the statement of profit and loss or to retained earnings.

The Bank reviews, in each reporting period, the need to record impairment of its investment in companies included on equity basis - see paragraph U below.

4. International Financial Reporting Standards (IFRS) on consolidating financial statements and related issues

Pursuant to a circular of the Supervisor of Banks of 1 January 2013, banks are required to implement a new system of standards on consolidating financial statements and related issues. Among others, IFRS 10 was adopted on Consolidated Financial Statements, except for the rules relating to the treatment of variable interest entities (VIE's). In addition, IAS 28 - Investments in Associates and Joint Ventures was adopted, and IFRS 12 - Disclosure of Interests in Other Entities, except for requirements included regarding structured entities that are not consolidated.

The Bank implemented the standards as of 1 January 2013 and thereafter on a retroactive basis.

Implementation of the system of standards did not have a material effect on the financial statements of the Bank.

Note 1 – Significant Accounting Policies (cont'd)

G. Basis of recognition of income and expenses

Income and expenses are included on an accrual basis, except for the following:

- Income and expenses from securities held for trading and derivative financial instruments are recognized according to the changes in fair value.

- Interest accruing on problematic debts that were classified as non-accrual loans is recognized on a cash basis when there is no doubt with regard to collection of the remaining recorded debt balance of an impaired debt. In these situations, an amount collected on account of the interest that is recognized as interest income, is limited to the amount that would be accumulated in the reporting period on the remaining recorded balance of the debt according to the contractual interest rate. Interest income on a cash basis is classified in the statement of profit and loss as a interest income under the relevant heading. When there is doubt as to collection of the remaining recorded balance of debt, all payments collected serve to reduce the loan principal. In addition, interest on past-due amounts in respect of housing loans is recognized in the profit and loss statement on an actual collection basis.

- Income from commissions on early repayment of loans, after deducting a relative portion relating to the financial equity, are included in the profit and loss statement in equal annual amounts during the period of the remainder of the period until repayment of the loan or for three years from the date of early repayment, whichever period is shorter.

- Allocation fees for credit facilities, together with commissions on financing business, are recognized in the statement of profit and loss relative to the periods of the transactions.

- Operating commissions for granting services are charged to profit and loss when the service is granted.

- In successive periods of an impairment which is other than of a temporary nature, interest income from investments in debt instruments will be recognized in the following way:

  Beneficial interests acquired or beneficial interests that have continue to be held by the Bank in the securitization of financial assets, which are accounted for using the prospective interest method – the excess of the amount of expected cash flows to be collected over the fair value of the debt instrument will be recognized as interest income over the remaining life of the debt instrument. In rare instances in which the Bank has no reasonable estimate with regard to amounts and timing of expected cash flows to be collected from the debt instruments, the Bank recognizes income using the cost recovery method or recognizes income on a cash basis.

  Other debt instruments – Income in the reporting period is accrued on the basis of the excess of expected cash flows of the debt instrument. (The base amount of the debt instrument at the date of impairment in value which is of a nature other than temporary constitutes its fair value).

H. Fair Value

Effective 1 January 2011, the Bank implements the rules set out in FAS 157 (ASC 820) that defines fair value and establishes a consistent working framework for the measurement of fair value by defining fair value assessment techniques with regard to assets and liabilities, and by establishing a fair value hierarchy and detailed instructions for implementation. In addition, as of 1 January 2012, the Bank applies the directive of the Banking Supervision Department on Fair Value Measurement that integrates the principles set out in Accounting Standards Update ASU 2011-04 on Fair Value Measurement in the Public Reporting Directives.

Note 1 – Significant Accounting Policies (cont'd)

Fair value is defined as the price that would be received when selling an asset or that would be paid to transfer a liability in a transaction between a willing seller and a willing buyer at the measurement date. The Standard requires, *inter alia*, for purposes of fair value valuation, making optimum use of observable inputs, and minimizing the use of unobservable inputs. Observable inputs provide information available to the market received from independent sources, whereas unobservable inputs reflect assumptions by the banking corporation.

FAS 157 stipulates a hierarchy of measurement techniques based on the determination if the inputs used for purposes of determining fair value are observable or unobservable. These types of input create a fair value hierarchy detailed as follows:

- Level 1 inputs: quoted prices (not adjusted) in active markets for identical assets or liabilities.

- Level 2 inputs: prices quoted for similar assets or liabilities in active markets; prices quoted for identical assets or liabilities in inactive markets; prices derived from evaluation methods in which all the significant inputs are observable in the market, or are supported by observable market data.

- Level 3 inputs: unobservable inputs for the asset or the liability deriving from evaluation model for which one or more of the significant inputs are not observable.

This hierarchy requires the use of observable market data, where such exist. When this is possible, the Bank considers relevant observable data in its evaluation, the scope and frequency of the transactions, the size of the bid-ask margin, and the size of adjustment required when comparing similar transactions, are all factors taken into account when determining the level of market liquidity and the degree of relevance of observable prices in those markets.

The level in the scale of fair value to which the fair value measurement of the financial instrument belongs is to be determined on the basis of the lowest level of the figure that is significant for the fair value measurement as a whole.

The Standard requires the banking corporation to reflect credit risk and non-performance risk in the measurement of the fair value of debt, including derivative instruments, issued by the banking corporation and measured at fair value. Non-performance risk includes the credit risk of the banking corporation, but is not limited to this risk only.

For further details regarding the methods and main assumptions used for purposes of assessing the fair value of financial instruments, see Note 18.D below, under the subject of balances and fair value measurements of financial instruments.

Methods of assessment implemented by the Bank for measuring fair value are evaluated taking into consideration the relevant circumstances for the various transactions, including prices of recent transactions in the market, indicative prices of assessment services, and the results of back-testing of similar types of transactions.

In addition, fair value measurement of financial instruments is made without taking into account the factor of the size of the holding with regard to financial instruments assessed in accordance with data of each of the levels, except for situation in which the premium or discount were taken into account in fair value measurement by market participants in the absence of Level 1 data.

Securities

The fair value of securities held for trading and securities available for sale is determined based on market prices quoted in the principal market. In those cases where a quoted market price is not available, the fair value is based on the best available information with maximum use of observable data and taking into account the risks inherent in the financial instrument. Fair value is determined using generally accepted pricing models, based on evaluations obtained from experts in valuing financial instruments or based on an independent system of the Bank. Evaluation methods include the use of various parameters, such as interest curves, currency rates and standard deviations, taking into account the risks inherent in the financial instrument (market risk, credit risk, non-marketability, etc.).

Most of the portfolio is calculated each month by a well-known international institution which is engaged in the calculation of fair value and is independent of the issuing entities and the marketing entities. The calculation is based mainly on the prices of transactions in active markets. The balance of the portfolio is revalued based on quotes from brokers or from the makers of the instruments, or based on the Bank's system.

Derivative financial instruments

The fair value of derivative financial instruments that have an active market is determined based on market prices quoted in a principal market.
In those cases where a quoted market price is not available, a fair value estimate is made by using models that take into account the risks inherent in the derivative instrument.

Non-derivative financial instruments

For most financial instruments in this category there is no active market in which they are traded. Accordingly, fair value is estimated using generally accepted pricing models, such as the present value of future cash flows discounted at an interest rate reflecting the level of risk inherent in the financial instrument. For this purpose, pursuant to Banking Supervision Department instructions, future cash flows for impaired debts and other debts have been calculated after deducting the effect of accounting write-offs and allowances for credit losses in respect of the debts.

The Fair Value Option for Financial Assets and Financial Liabilities

FAS 159 (ASC 825-10) allows a banking corporation to elect, on defined dates, to measure financial instruments and certain other items (the eligible items) at fair value, which under the Public Reporting Directives are not required to be measured at fair value. Unrealized profits and losses in respect of changes in the fair value of the items for which the fair value alternative is selected, shall be reported in the statement of profit and loss for each consecutive reporting period. In addition, prepaid costs and fees related to the items for which the fair value alternative is selected, shall be recognized in profit and loss on the date of creation, rather than deferred. The election to apply the fair value alternative, as noted above, shall be made instrument by instrument, and cannot be cancelled. In addition, FAS 159 establishes presentation and disclosure requirements aimed at facilitating comparisons between banking corporations that choose different bases for measurement of similar types of assets and liabilities.

Notwithstanding the above, it is clarified by the Banking Supervision Department that a banking corporation shall not elect the fair value alternative unless it has developed prior know-how, systems, procedures, and controls at a high level, which will enable it to measure the item to a high degree of reliability. Thus, a banking corporation shall not elect the fair value alternative with regard to any asset requiring classification as level 2 or level 3 of the fair value hierarchy, or with regard to any liability, unless it receives prior approval to do so from the Banking Supervision Department.

I. Impaired Debts, Credit Risk and Allowance for Credit Losses

The Bank applies the Directive of the Supervisor of Banks on Measurement and Disclosure of Impaired Debts, Credit Risk, and the Allowance for Credit Losses as of 1 January 2011.
The Directive has been implemented with regard to all debt balances such as deposits in banks, bonds, securities borrowed or purchased under repurchase agreements, credit to the public, credit to the government, etc. Credit to the public and other debt balances for which no specific rules were made in the Public Reporting Directives regarding the measurement of the allowance for credit losses (such as

credit to the government, deposits in banks, etc.) are reported in the books of the Bank according to the recorded debt balance. It should be explained that prior to 1 January 2011, the Bank applied different rules according to which the debt balance in the Bank's books included the interest component accumulated before the debt was classified as a non-income bearing troubled debt. Accordingly, and in light of credit balances written off in accordance with the new directives, loan balances reported in periods before the initial implementation period of the Directive are not comparable with loan balances reported after the commencement of implementation. With regard to other debt balances, for which there are specific rules for measurement and recognition of impairment (such as bonds), the Bank continues to apply the same rules for measurement.

The Bank has decided on the procedures required to maintain an allowance for credit losses at a level appropriate to cover expected credit losses relating to its loan portfolio, including in respect of off-balance sheet credit risk. Allowances for credit losses include:

- Individual allowance for credit losses – The allowance is made based on the measurement of the impairment of the debt, based on the present value of future expected cash flows, discounted at the effective rate of interest of the debt; or, when a debt is dependent on collateral or when an asset is expected to be seized, according to the fair value of the collateral pledged to secure such credit (less costs of sale). The need for an individual allowance is assessed for each obligo whose contractual balance (without deducting: accounting write-offs not involving a legal waiver, interest not recognized, allowances for credit losses, and collateral) is NIS 1 million or more, and any other debt identified for individual assessment by the Bank. In some of the consolidated subsidiary companies, the assessment is made also for lower amounts. The individual allowance is calculated for each debt classified as impaired (see below).

  Collective allowance for credit losses – This is implemented for large groups of relatively small and homogeneous debts, and in respect of debts that have been assessed individually and found not to be impaired. Measurement of credit losses is based on the principles set out in FAS 5 (ASC 450) – Accounting for Contingencies and on the transitional directives set out below. The allowance assessed on a group basis for off-balance sheet credit instruments is based on the rates of allowance determined for balance sheet credit, taking into account the percentage of off-balance sheet credit risk expected to be realized. The credit realization percentage is calculated by the Bank based on credit conversion coefficients as set out in Proper Conduct of Banking Business Directive No. 203 – Measurement and Adequacy of Capital – Credit Risk – Standardized Approach, with certain adjustments in cases where the Bank has prior experience indicating percentages for the realization of credit.

  A temporary directive was issued for the years 2011-2013 (hereinafter: “the transitional period”), for calculating credit loss allowances on a collective basis. According to the temporary directive, the rate of allowances for credit losses on a collective basis will be determined for the transitional period based on the range of historical rates for provisions for doubtful debts during the years 2008-2010, segmented by sector of the economy, as well as on the actual rate of net accounting write-offs as of 1 January 2011. In addition to calculating the range of historical rates in the various sectors of the economy as mentioned above, the Bank, for purposes of determining the appropriate rate of the provision, takes into account other data, including conditions of the sector, macroeconomic data, a general assessment of the quality of credit to sectors of the economy, changes in volume and the trend of balances in arrears and impaired balances, and the effect of the changes on credit concentrations.

  The minimum provision for doubtful debts in respect of housing loans is calculated according to a formula determined by the Supervisor of Banks, taking into account the extent of arrears, whereby the rates of the provision increase as the arrears grow. The application of the calculation of the provision according to the formula of the extent of arrears refers to all housing loans, except for loans not payable in regular installments and loans financing activity of a business nature.

Similarly, a provision is made on the balance of housing loans not in arrears based on past statistics.

In addition, the Bank implemented the provisions of a letter from the Supervisor of Banks regarding the updating of guidelines on residential property. The Bank formulated a policy designed to ensure that it complies with the new requirements that, as of 31 March 2013, the balance of the collective allowance for credit losses for housing loans will not be less than 0.35% of the balance of the said loans at the reporting date.
The Bank implemented the guidelines in the first quarter of the year resulting in an increased provision in respect of housing loans for which there is no allowance by extent of arrears or a specific allowance assessed on an individual basis in the amount of NIS 50 million charged to profit and loss.

On 18 July 2013 a draft was forwarded for discussion to the Advisory Committee on "Collective Allowance for Credit Losses". For further details see paragraph X.3 below.

The Bank examines the overall appropriateness of the allowance for credit losses based on management's judgment, taking into account the risks inherent in the loan portfolio.

The Bank also calculates a supplementary and general provision under the policy for the provision for doubtful debts before the implementation of the directives on impaired debts, credit risk, and the allowance for credit losses.
These provisions are used only as an indicator for the collective allowance such that if the total collective allowance is less than the supplementary and general provision, the allowance is to be made using the higher of the two calculations.

Classification of troubled debts

The Bank determined procedures for identifying problem troubled credit and classifying debts as impaired. In accordance with these procedures, the Bank classifies the balance of its various troubled debts as follows: special mention, substandard, or impaired.

Special mention credit
Special mention balance sheet credit is a debt which has potential weaknesses in respect of which special attention is required by the management of the corporation. Off-balance sheet credit is classified as special mention credit if realization of the liability contingent on this item is "possible", and if the debts which may be recognized as a result of the contingent realization are suitable for classification in this category.

Substandard credit
Substandard balance sheet credit is credit which is insufficiently protected by the current established value and the debtor’s repayment ability, or by the pledged collateral, if any. Balance sheet credit risk classified as such has a well-defined weakness or weaknesses that put the realization of the debt at risk. Credit for which an allowance for credit losses is recognized on a collective basis will be classified substandard when it becomes a debt with arrears of 90 days or more.

Impaired credit

Identifying and classifying impaired credit
Impaired debt is credit of which the banking corporation, based on current information and events, will probably not be able to collect the entire amount due (principal and interest), according to the contractual terms of the loan agreement. In particular, a debt is classified as impaired when its principal or interest is in arrears of more than 90 days, except if the debt is well secured or in collection proceedings. In addition, an impaired debt is also considered as a debt whose terms were changed due

to troubled debt restructuring, unless prior to and after the restructuring a minimum allowance was made for credit allowance by extent of arrears.

Changing an impaired debt back to non-impaired status
An impaired debt reverts to being classified as a non-impaired debt if one of the two following conditions is met:

1. There are no components of principal or interest in regard thereof repayment has become due but have not been paid, and the Bank expects repayment of the remaining principal and interest in full under the terms of the contract (including accounting write-offs or amounts that have been provided for).

2. When the debt has become well-secured debt and is in process of collection.

Changing an impaired debt back to an impaired accrual status
A debt for which after restructuring there is reasonable certainty that it will be repaid in accordance with its new terms, is changed back for treatment as a debt accruing interest income under terms of restructuring, and any accounting write-off carried out in the debt is supported by an updated appraisal as to the financial condition of the debtor, based on continuous repayment performance of at least six months.

Troubled debt restructuring
A debt which formally underwent a troubled debt restructuring is defined as a debt in respect of which, for economic or legal reasons related to the debtor's financial difficulties, the Bank granted a waiver by way of modification of the terms of debt, in order to alleviate the burden for the debtor of near-term cash payments or by way of receipt of other assets as payment of the debt. For purposes of determining whether a debt agreement executed by the Bank comprises a troubled debt restructuring, the Bank performs a qualitative examination of the totality of the terms of the arrangement and the circumstances under which it was made, in order to determine whether (1) the debtor is in financial difficulties and (2) the Bank granted a waiver under the arrangement to the debtor.

In order to determine whether the debtor is in financial difficulties, the Bank examines whether there are signs that point to the fact that the borrower is in difficulties at the time of the arrangement or the existence of a reasonable possibility that the borrower would get into financial difficulties if not for the arrangement.

The Bank examines, *inter alia*, the existence of one or more of the following circumstances:

- At the time of the debt arrangement the borrower is in default, including when any other debt of the borrower is in default;

- With regard to debts which at the time of the arrangement are not in arrears, the Bank estimates if according to the current repayment ability it is likely that in the foreseeable future the borrower will get into a default situation, and will not meet the original contractual terms of the debt;

- The debtor was declared bankrupt;

- Is under receivership, or there are significant doubts as to the borrower's continued existence as a going concern;

- And that without changing the terms of the debt, the debtor will not be able to raise debt from other sources at market rates of interest for debtors not in default.

- The debtor was granted a waiver, even if under the arrangement an increase was made in the contractual interest rate, if one or more of the following situations exist:

Note 1 – Significant Accounting Policies (cont'd)

- As a result of restructuring, the Bank is not expected to collect all amounts outstanding (including accrued interest according to the contractual terms);
- The updated fair value of the collateral, in respect of debts conditional on collateral, does not cover the contractual balance of the debt and indicates the inability to collect all amounts due;

- The debtor has no possibility of raising resources at the rate prevailing in the market for a debt with terms and characteristics such as those of the debt granted under the arrangement.

In addition, the Bank will not classify debt as a restructured troubled debt if, under the arrangement, the debtor was granted a stay of payments that is not material, given the frequency of the payments in the contractual repayment period and the expected duration of the original debt. In this regard, if several arrangements were made involving changes in the terms of the debt, the Bank takes into account the cumulative effect of the previous arrangements for the purpose of determining whether the stay of payments is not material.

Restructured debts, including those that prior to the restructuring were examined on a group basis, will be classified as impaired debt and will be evaluated on an individual basis for purposes of making an allowance for credit losses, or an accounting write-off. Given that the debt, for which the troubled debt restructuring was carried out, will not be paid in accordance with its original contractual terms, the debt continues to be classified as impaired debt, even after the debtor returns to the repayment schedule in accordance with the new terms.

Recognition of income:

At the time the debt is classified as impaired, the Bank defines the debt as a debt not accruing interest income, and ceases accruing interest income on it, except that stated above regarding certain impaired debts after restructuring. In addition, at the time the debt is classified as impaired, the Bank cancels all the interest income accrued but not yet collected, which was recognized as income in profit and loss. The debt remains classified as a debt not accruing interest income, as long as the impaired debt classification is not canceled. A debt that underwent a formal troubled debt restructuring, and after the restructuring there is reasonable certainty that the debt will be repaid and will perform in accordance with its new terms, will be treated as an impaired debt accruing interest income. For details regarding recognition of income on a cash basis for debts classified as impaired, see paragraph G.

Regarding debts assessed and provided for on a collective basis, which are in arrears of 90 days or more, the Bank continues to accrue interest income. These debts are subject to methods of evaluation for the allowance for credit losses that ensure that the profit of the Bank is not overstated. Late-payment commissions for these debts are included as income on the date the Bank becomes entitled to receive them from the customer, provided that collection is reasonably secured.

Accounting write-off

The Bank makes an accounting write-off in the cases set out below:

- Any debt or part thereof examined on an individual basis that is considered uncollectible, or a debt which the Bank has made efforts to collect over an extended period.

- A debt in respect of which the Bank is making efforts to collect the debt and for which individual allowances for credit losses have been made, generally within a period not exceeding two years.

- In the event of a debt whose collection in collateral-contingent, any part of a debt which exceeds the value of the collateral, which is identified as uncollectible will be written off immediately against the allowance for credit losses.

- Troubled debts in respect of which the allowance is measured based on a collective allowance for credit losses when the period of arrears exceeds 150 days.

It should be explained that accounting write-offs do not involve a legal waiver, and they reduce the reported balance of debt for accounting purposes only, while creating a new cost base for the debt in the Bank's books.

Doubtful Debts Provision Policy before the Implementation of the Directives on Impaired Debts, Credit Risk, and Allowance for Credit Losses

Provisions for doubtful debts were determined specifically, together with a general and a supplementary provision, in accordance with directives of the Supervisor of Banks. Provisions for doubtful debts in consolidated banking companies overseas were determined in accordance with generally accepted principles in their country of domicile.

The specific provision for doubtful debts was made based on a careful assessment by management of losses inherent in the loan portfolio, including debts in non-balance sheet items. In this assessment, management took into account, among its other considerations, to what degree the risks were connected to the financial strength of the borrowers, based on information available to it regarding their financial condition, business activity, compliance with their obligations, and an assessment of the value of the collateral received from them.
Interest income in respect of a loan determined as doubtful was not recorded from the beginning of the quarter in which the debt was determined as doubtful. When the interest was collected, the interest income was recorded under other financial income.

A specific provision for housing loans granted by the Bank and investee banking companies in Israel is calculated in accordance with the directives of the Supervisor of Banks, taking into account the length of the period in arrears, with the rates of the provision increasing as the arrears increase.

The supplementary provision for doubtful debts was based on the quality of the customer credit portfolio, according to risk characteristics defined in the directives of the Supervisor of Banks. Different provision percentages were stipulated for each of the risk characteristics. The supplementary provision for doubtful debts was calculated according to percentages stipulated for the various characteristics. The general provision was in figures adjusted to the end of 2004, in an amount comprising 1% of total liabilities under the responsibility of the Bank and its investee banking companies as at 31 December 1991.

Initial implementation of the directives of the Supervisor of Banks regarding updating the disclosure on credit quality of debts and the allowance for credit losses

The Bank implements the provisions of a circular of the Supervisor of Banks regarding updating the disclosure on credit quality of debts and the allowance for credit losses for the adoption of Accounting Standards Update ASU 2010-20 which requires wider disclosure obligations regarding debt balances, changes in the balance of the allowance for credit losses, any material purchases and sales of debts during the reporting period, and disclosures on credit quality.

In addition, disclosure is to be included on the credit quality of housing loans, a new disclosure for each of the credit segments and for each of the primary groups of debts as defined in the Directive, distinguishing between borrower activities in Israel and borrower activities abroad if material.
The Group applies the provisions as from 1 January 2012 prospectively for the balance sheet data required for the first time by this Directive, while reclassifying comparative figures as far as possible. Other disclosures required by this directive will be implemented as of the financial statements at 31 March 2013 and thereafter.
First-time implementation of the directive had no effect other than a change in presentation.

Note 1 – Significant Accounting Policies (cont'd)

J. Securities

1. Securities in which the Bank invests are classified in three portfolios as follows:

a. Debentures held to maturity

Debentures which the Bank intends and is able to hold until redemption date. Debentures held to maturity are stated at cost with the addition of accrued interest, linkage and foreign currency differences, taking into consideration the proportion of the premium or discount and less provision for impairment in their value which is not of a temporary nature.

b. Securities held for trading

Securities which were acquired and are held with the aim of selling them in the near future, and securities for which the banking corporation chose to make fair value measurement through the statement of profit and loss. Securities held for trading are stated at fair value at the reporting date. Unrealized gains and losses are included in the statement of profit and loss.

c. Securities available for sale

Securities not classified as debentures held to redemption or as securities held for trading. Securities available for sale are stated in the balance sheet at their fair value on the reporting date, except for shares, options and venture capital funds in respect of which the fair value is not available, in which case they are stated at cost.

Differences between the fair value and the amortized cost, less a reserve for tax, are shown in a separate item within shareholders' equity, under other comprehensive profit. Impairment in value which is not of a temporary nature is charged to the profit and loss statement as detailed in paragraph 3 below.

Unrealized gains or losses from adjustments to fair value of securities available for sale designated as being hedged by fair value hedges, are charged to the statement of profit and loss over the period of hedge.

2. Dividend income, accumulated interest, linkage and price differences, amortization of premium or discount (in accordance with the effective interest method), as well as losses from impairment in value not of a temporary nature, are recorded to the profit and loss statement.

3. Interest income in respect of beneficial interests which have been acquired, such as asset-backed financial instruments, e.g., MBS, CLO, SCDO and CMO (except for high-quality loan instruments) is recognized using the prospective interest method (future interest that also anticipates future changes) , adjusting the interest rate used for recognizing interest for changes in the estimate of future cash flows. High quality loan beneficial interests are beneficial interests issued under the guarantee of the United States government or agencies of the U.S. government, and asset-backed securities whose international credit rating is at least AA.

4. The Bank's investments in venture capital funds are dealt with according to cost less losses from impairment of a nature other than temporary. Profits from venture capital investments are credited to the profit and loss statement when the investment is realized.

Note 1 – Significant Accounting Policies (cont'd)

5. Fair Value

With regard to the determination of fair value, see paragraph H below.

6. Impairment

The Bank examines the necessity, in each reporting period, for making a provision for impairment of securities which is not of a temporary nature. The examination is carried out if there are indications that the value of the securities might be impaired. The criteria for determining if the impairment is not of a temporary nature are based on the following considerations and tests:

- Intention and ability to hold the security until the forecasted recovery in full of the cost.
- The assets and collaterals backing up the security.
- The percentage of impairment from the cost of the security.
- Duration of period in which the fair value of the security is lower than cost.
- Evaluation of repayment ability and rating.
- An adverse change in the situation of the issuer or in the state of the market as a whole.

The Bank's policy is to recognize the impairment of a security as having a nature other than temporary, at least in respect of the impairment of any security that fulfils one or more of the following conditions:

- A security which was sold before the publication of the report to the public.
- A security which the Bank intended to sell within a short period of time before the publication of the report to the public.
- A debenture for which there was a significant rating decrease between the rating of the debenture at the date of acquisition by the Bank and the rating of the debenture at the date of publication of the report. Only a rating decrease below BBB- is considered a significant rating decrease for purposes of this paragraph.
- A debenture which was classified as problematic by the Bank after its acquisition.
- A debenture in respect of which there was a credit failure which was not rectified within a reasonable period of time.
- A security whose fair value was lower than the purchase value for a period of time of at least nine months before the end of the period of the financial statement, and at the end of the statement period as well as at a date shortly before publication of the report was lower by 35% or more than the cost (in the case of a debenture – the depreciated cost). In this matter an exception is possible if the Bank has concrete objective evidence and a conservative analysis of all the relevant factors, to show with a high degree of certainty that the impairment is of a temporary nature. The objective evidence and the relevant factors include parameters such as: an increase in value after the date of the financial report, a high credit rating (group A or above), an analysis of stability in stress scenarios carried out by an independent external party or by the Bank, backing and direct government investment in shareholders' equity for purposes of ensuring the strength of the issuer.

  These principles are in accordance with the guideline issued by the Supervisor of Banks, except for the definitions of "significant rating" and "significant impairment" which were determined by the Bank.

  When impairment in value occurs not of a temporary nature, the cost of the security is reduced to the fair value and serves as a new cost basis. Losses from securities which are not of a temporary nature are charged to the statement of profit and loss. Increases in value over the new cost basis in subsequent reporting periods, are included in a separate item in shareholders' equity under total other accumulated profit and is not charged to profit and loss.

K. Derivative financial instruments including hedge accounting

The Bank holds derivative financial instruments for purposes of hedging foreign currency risks and interest rate risks, and also carries out activity in derivatives not for hedging purposes, including embedded derivatives that have been separated.

If an instrument is earmarked for hedging, the Bank, at the date the hedge is made, formally documents the hedging relationships between the hedging instrument and the hedged item, including the purpose of risk management and the Bank's strategy in creating the hedging transaction, and the manner in which the Bank will evaluate the effectiveness of hedging relationships. The Bank evaluates the effectiveness of hedging relationships both at the beginning of the hedge and also on an ongoing basis. In addition, the Bank applies hedge accounting in the "shortened" version which assumes full effectiveness in accordance with the provisions of the standard.

1. Fair value hedging

Changes in the fair value of derivative financial instruments designated to hedge fair value are charged to the profit and loss statement. The hedged item is also shown at fair value with reference to the risks hedged, and changes in fair value are charged to the profit and loss statement.

If the hedging instrument no longer fulfills the criteria of an accounting hedge, or expires, is sold, cancelled or realized, or the Bank cancels the designation of a fair value hedge, the Bank ceases utilization of hedge accounting. When a hedged firm commitment no longer fulfills the definition of a firm commitment, any asset or liability recorded in accordance with recognition of the firm commitment will be cancelled and recognized immediately and on a current basis in the statement of profit and loss.

Hedging a net investment in a foreign operation – see paragraph E.

2. Asset and liability management

Hedge accounting is not applied with regard to derivative instruments serving as part of the Bank's asset and liability management system (ALM). Changes in the fair value of these derivatives are recognized in the statement of profit and loss when incurred.

3. Other derivatives

Changes in the fair value of derivatives not used for hedging or covering exposures are charged immediately to profit and loss.

4. Embedded derivatives

Embedded derivative instruments are separated from the host contract and dealt with separately if: (a) there is no clear and close relationship between the economic characteristics and risks of the host contract and of the embedded derivative instrument, including credit risks attributable to certain embedded credit derivatives; (b) a separate instrument with the same conditions as the embedded derivative instrument would fulfill the definition of a derivative; and (c) the hybrid instrument is not measured according to fair value through profit and loss.

An embedded derivative that was separated is included in the balance sheet together with the host contract, and changes in fair value of separated embedded derivatives are charged on a current basis to profit and loss.

In certain cases (such as in cases when the Bank is not able to separate the embedded derivative from the host contract), pursuant to American Accounting Standard (FAS 155), Accounting Treatment of Certain Hybrid Financial Instruments, the Bank elects not to separate the embedded derivative and to measure the hybrid instrument as a whole for fair value while reporting on changes in the fair value in the statement of profit and loss when they occur. The above election is made at the date of purchase of the hybrid instrument or on the occurrence of certain events when the instrument is subject to re-measurement (a re-measurement event), such as a result of business combinations or material changes in the debt instrument. Such fair value election is irrevocable.

5. Fair value

With regard to the determination of fair value, see paragraph H above.

L. Transfers and Servicing of Financial Assets and Extinguishments of Liabilities

The Bank applies the measurement and disclosure principles prescribed in US Accounting Standard FAS 140 (ASC 860-10) - Transfers and Servicing of Financial Assets and Extinguishments of Liabilities, amended by FAS 166 (ASC 860-10) - Transfers and Servicing of Financial Assets, for the purpose of dealing with transfers of financial assets and extinguishment of liabilities. In accordance with these principles, the transfer of a financial asset will be accounted for as a sale, if and only if, all of the following conditions are fulfilled: (1) the transferred financial asset has been isolated from the transferor, both in a state of bankruptcy or other receivership; (2) any recipient (or, if the recipient is an entity whose sole purpose is to engage in securitization or asset-backed financing activities and that entity is constrained from pledging or exchanging the financial assets it receives, each third-party holder of its beneficial interests) can pledge or exchange the assets (or beneficial interests) it received, and no condition exists that also constrains the recipient (or a third-party of its beneficial interests) from taking advantage of its right to pledge or exchange and provides the transferor with more than a trivial benefit; (3) the transferor or consolidated companies included in its financial statements or its agents do not maintain effective control over the financial assets or beneficial interests relating to the transferred financial assets.

As of 1 January 2012, the Bank applies Accounting Standards Update ASU 2011-03 – "Reconsideration of Effective Control for Repurchase Agreements".

In contractions for the transfer of financial assets, the Bank determines that effective control of the assets transferred remains with the transferor if the following conditions are met:

- The assets to be repurchased or redeemed are the same or substantially the same as those transferred;
- The agreement is to repurchase or redeem them before maturity, at a fixed or determinable price;
- The agreement is entered into contemporaneously with the transfer.

In addition, in order for the transfer of some of the financial asset to be considered a sale, the part transferred must comply with the definition of participating interests. Participating interests must comply with the following criteria: the interest must represent a proportionate interest in relation to an entire financial asset; all cash flows received from the assets are divided proportionately among the participating interest holders in an amount equal to their share of ownership; the rights are not subordinated rights in relation to other rights; there is no right of recourse to the transferor or to other holders in participating interests (other than in the event of a breach of representations or warranties, ongoing contractual obligations to service the entire financial asset and administer the transfer contract, and contractual obligations to share in any set-off benefits received by any holder of participating interests); and neither the transferor, nor the participating interest holder has the right to pledge or exchange the entire financial asset, unless all participating interest holders agree to pledge or exchange the entire financial asset.

If the transaction meets the conditions for treating a transaction as a sale, the transferred financial assets are deducted from the Bank's balance sheet. If the sale conditions are not fulfilled, the transfer is considered a secured debt. A sale of part of a financial asset which is not a participating interest as defined below is treated as a secured debt, i.e., the transferred assets continue to be recorded in the Bank's balance sheet and the proceeds from the sale will be recognized as a liability of the Bank.

Securities sold under conditions of repurchase or purchased under conditions of resale, securities borrowed or lent, and other financial instruments transferred or received by the Bank, in which the Bank did not lose control over the transferred asset or did not acquire control in the asset received, are treated as secured debt. Financial instruments transferred in transactions such as the above, are measured in accordance with the same principles applied before their transfer.

Securities sold as mentioned above are not deducted from the balance sheet and are shown under "Securities", and as opposed to these, the deposit, for which those securities were pledged to ensure its repayment, is shown under "Securities lent or sold under agreements to repurchase".

Securities purchased are recorded according to their value on the day the transaction was made under "Securities borrowed or purchased under agreements to resell".

The Bank monitors the fair value of securities borrowed and lent as well as securities transferred under purchase and resale agreements on a daily basis, and a demand for collateral is made in appropriate cases. Interest received or paid in respect of the said securities is reported under net interest income (expense).

Pursuant to the directives of the Supervisor, securities lending transactions executed as "ordinary" credit transactions, in which the Bank lends securities against the collateral portfolio, and the borrower does not provide the banking corporation with a security margin relating specifically to the securities lending transaction, are shown as credit to the public according to market value and are added to the debt of the borrower. Changes in the value of the above securities on an accrual basis are shown in the profit and loss statement under interest income from credit to the public, and the adjustment to market value is shown under adjustments in respect of securities available for sale according to fair value.

The Bank deducts a liability if and only if the liability is repaid, i.e. one of the following conditions exist: (a) the Bank paid the lender and was released from its obligation under the liability, or (b) the Bank was legally released, by legal proceedings or by agreement of the lender, from being the principal debtor under the liability.

M. Offsetting assets and liabilities

The Bank implements the rules set out in the circular of the Supervisor of Banks dated 12 December 2012, updating the Public Reporting Directives of the Supervisor of Banks regarding offsetting assets and liabilities.

The Bank offsets assets and liabilities arising from the same counterparty and reports their net balance in the balance sheet, if the following cumulative conditions are met:

- In respect of those liabilities, there is a legally enforceable right to offset the liabilities from the assets.

- There is an intention to repay the liabilities and realize the assets on a net basis or simultaneously.

- Both the Bank and the counterparty owe each other determinable amounts.

The Bank offsets assets and liabilities with two different counterparties and reports a net balance in the balance sheet if the above two cumulative conditions are met, and provided that there is an agreement between the three parties that clearly defines the Bank's right of offset in respect of those liabilities.

The Bank offsets deposits whose repayment to the depositor is contingent on the extent of collection of the credit and the credit that was granted from these deposits, with the Bank having no risk of loss from the credit. The margin on this activity is included under "Commissions".

The Bank offsets between derivative instruments made with the same counterparty which is subject to a master netting arrangement. The offset is carried out only for purposes of calculating the indebtedness of the customer reported in the various notes.

The Bank implements the rules included in the directives retroactively from 1 January 2013. First time implementation did not have any material effect on the financial statements of the Bank other than updating the disclosure format in Note 18.D on Activity in Derivative Instruments – Scope, Credit Risks and Repayment Dates, as required in the directive.

N. Buildings and equipment

Recognition and measurement

Buildings and equipment are shown at cost less accumulated depreciation and losses from impairment in value. Cost includes expenses which can be directly attributed to acquisition of the asset.

When significant parts of fixed assets have a different life span they are dealt with as separate items of fixed assets.

Buildings earmarked for sale are shown at the lower of cost or realizable value.

Profit or loss on the sale of fixed assets is included under "Other income" in the statement of profit and loss.

Subsequent costs

The cost of replacement of part of an item of fixed assets is recognized as part of the book value of that item if it is expected that the future economic advantages inherent in the part replaced will come to the Bank, and if its cost can be measured accurately. The book value of the part replaced is deducted in the books. Ongoing maintenance costs of fixed asset items are charged to the profit and loss statement when incurred.

Costs of software

Pursuant to the Public Reporting Directives, the Bank classifies under this section the costs in respect of software assets acquired or costs capitalized as an asset in respect of software developed internally for its own use.

Software purchased is measured by costs less accumulated depreciation and losses from impairment in value.

Costs in connection with the development and adaptation of computer software intended for internal use are capitalized only if development costs can be measured reliably, the software can be implemented from a technical point of view, a future economic advantage is expected and the Bank has both an intention and sources of funds to complete the development and use the software. Capitalized costs include direct costs and overhead expenses which can be attributed directly to the preparation of the software for its intended use. These costs are measured by cost less accumulated depreciation and losses from impairment in value. Other costs are charged to profit and loss when incurred.

Subsequent costs of software are recognized as an asset only if they increase the future economic advantages inherent in the asset for which they were expended. Other costs are charged to profit and loss when incurred.

Depreciation

Depreciation is calculated on the cost, in accordance with estimated useful life, on a straight line basis from the date the asset is ready for use. The Bank depreciates separately each part of a fixed asset for which a different useful life has been determined. Leasehold improvements are amortized over the leasing period, including an option which is likely to be exercised, or over its useful life, whichever is shorter. An asset is amortized when it is available for use.
The estimates regarding useful life and residual value are examined periodically, and at least at the end of each financial year, and adjusted if necessary.

In connection with impairment of non-monetary assets, see paragraph U below.

Leases

Leases, including leases of land from the Israel Land Authority or other third parties, where the Group materially bears all the risks and returns from the property, are classified as finance leases. At the commencement of the initial lease term, leased assets are recognized at an amount equal to the lower of fair value and the present value of future minimum lease payments. Future payments for exercising an option to extend the period of the lease with the Israel Land Authority are not recognized as part of the asset and related liability to the extent their amount is derived from the fair value of the land at future renewal dates of the lease agreement. After initial recognition, the asset is dealt with in accordance with accepted accounting policy regarding this asset.

The period of the lease is the period which cannot be canceled, for which the lessor made a contractual agreement for the lease of the asset together with any additional periods for which the lessee has the option of continuing to lease the asset, for an extra payment or for no extra payment, when it is reasonable certain at the date of the leasing commitment that the lessee will exercise the option.

The other leases are classified as operating leases, and the leased assets in these cases are not recognized in the balance sheet.

Payments in the framework of an operational lease are charged to the statement of profit and loss on a straight-line basis over the term of the lease.

Investment Property

Investment property is real estate (land or buildings – or part of the same – or both) held by the Bank (as owners or under a financial lease) for purposes of generating rental income or for an increase in equity value or both, and not the purposes of:

1. Use for production or supply of goods or services for administrative purposes; or

2. Sale in the normal course of business.

Investment property is measured initially at purchase cost plus transaction costs. In subsequent periods, investment property is measured at cost less accumulated amortization and losses from impairment.

O. Issue expenses

Expenses of issue of debentures, bonds and subordinated notes are amortized by the effective interest method over the expected life of the instrument issued.

P. Assets transferred to Group ownership following the settlement of troubled debts

Assets that were transferred to Group ownership following the settlement of troubled debts and are included in other assets are stated according to the lower of the asset's fair value on the date they were transferred or fair value as at balance sheet date. Decreases in value are charged to operating and other expenses.

Q. Contingent liabilities

Appropriate provisions have been made for claims which, in the opinion of Bank Management and the Managements of its consolidated companies, based on the opinions of legal counsel, will not be dismissed or canceled, notwithstanding the fact that such claims are refuted by the Bank. In addition, there are legal proceedings whose chances or results cannot be estimated at this stage and therefore no provision was recorded in respect thereof.

Claims made against the Bank are classified in three categories, according to the probability of realization of the risk exposure as follows:

- Probable risk – probability of realization of the risk exposure exceeding 70%. For claims included in this risk group, appropriate provisions are included in the financial statements.

- Reasonably possible risk – probability of realization of the risk exposure between 20% and 70%. For claims included in this risk group, provisions are not included in the financial statements but only disclosure is made.

- Remote risk – probability realization of the risk exposure less than or equal to 20%. For claims included in this risk group, provisions are not included in the financial statements and no disclosure is made.

In rare cases where the Bank determines that, in the view of Bank Management, with reliance on its legal advisors, it is not possible to evaluate the likelihood of realization of the risk exposure with regard to a normal claim and a claim approved as a class action, no provision is made.

In addition, the Group is exposed to legal claims that have not yet been made / submitted, *inter alia*, on the existence of a doubt in the interpretation of an agreement and/or the provision of a law, and/or the method of their implementation. This exposure is brought to the Group's attention in a number of ways. In assessing the risk arising from the demands / claims not yet submitted, the Group relies on internal assessments of the officials dealing with the issues and the management, who weigh the assessment of the risk for submitting a claim, the chance of the claim's success, if it is submitted, and payment in a compromise, if there be any. The assessment is based on accumulated experience in relation to the submission of claims and on an analysis of claims in their own right. In the nature of things, in light of the preliminary stage of clarification of the legal claim, the actual result could be different from the assessment made at a stage prior to the claim being submitted.

In Note 18 details are shown of the amount of the additional exposure in respect of contingent claims whose amount exceeds NIS 2 million and whose realization is not remote, as well as a disclosure of material legal proceedings against the Bank and the consolidated companies.

Note 1 – Significant Accounting Policies (cont'd)

R. Employee rights

There are appropriate reserves for all liabilities regarding employer/employee relations, pursuant to the law, agreements, accepted practice and management's expectations. Future liabilities for pensions and jubilee grants are calculated by a qualified actuary, using the accrued benefit valuation method, taking into account probabilities based on past experience. The capitalization rate of the reserves is 4%, as determined by the Supervisor of Banks, the mortality rate is based on updated instructions including a circular of the Commissioner of Capital Markets, Insurance and Savings in the Ministry of Finance that was published on the matter. The rate of increase in salary is based on past experience and varies according to the age of the employee.
Liabilities for retirement compensation and pensions are covered mainly by allocated funds deposited in pension and retirement provident funds. In respect of those amounts not covered as stated, a provision is included in the financial statements; see Note 15 – Employee Rights. With regard to the matter of adoption of accounting principles in the U.S. on employee rights, see X.2.

Instructions and Clarifications on the Strengthening of Internal Control over Financial Reporting relating to Employee Rights

On 27 March 2011, instructions were published by the Banking Supervision Department on the strengthening of internal control over financial reporting relating to employee rights. The instructions provide a number of clarifications concerning assessing the liability in respect of employee rights, and instructions in the matter of internal control over the financial reporting process on the subject of employee rights, with a requirement for the engagement of a certified actuary, the identification and classification of liabilities in respect of employee rights, the maintaining of internal controls for purposes of reliance on the actuary's valuation and its validation, as well as certain disclosure requirements.

It was stipulated, *inter alia*, that a banking corporation expecting to pay its employees, on their leaving, benefits in excess of contractual terms, shall take into account the percentage of employees expected to leave and the benefits expected, for the calculation of pension and jubilee grant obligations. As a result of the above instruction, the Bank made an estimate of the number of employees expected to leave early in the actuarial models on which pension and jubilee grant obligations are based, and benefits in excess of contractual terms were taken into account.

Share-based payment transactions

Share-based payment transactions include transactions with employees that were settled with equity instruments. The fair value at the date that option and share warrants were granted to employees is attributed to salary expenses concurrently with an increase in capital over the course of the period during which the employees' entitlement to option and share warrants is attained. The amount attributed as an expense is adjusted in order to show option-warrants for shares which are expected to become vested. Fair value is determined by using an acceptable costing model. Deferred tax in respect of a share-based payment is calculated in accordance with the difference between the exercise price and the price of the share.

In transactions in which the Bank also grants rights to equity instruments to employees of the subsidiary companies, the Bank treats this as a share-based payment transaction settled with equity instruments.

S. Tax expenses on income

Taxes on income include current and deferred taxes. Current and deferred taxes are charged to the statement of profit and loss, unless the taxes derive from business combinations, or are charged directly to equity if they derive from items recognized directly in equity.

Note 1 – Significant Accounting Policies (cont'd)

Current taxes

Current tax is the amount of tax expected to be paid (or received) on income liable to tax for the year calculated at the applicable tax rates under laws that have been enacted or substantively enacted at the reporting date, including changes in tax payments relating to previous years.

The provision for taxes on the income of the Bank and its consolidated companies that are financial institutions for Value Added Tax purposes, include profit tax levied on the income according to the Value Added Tax Law. Value Added Tax Law levied on salaries in financial institutions is included in the statement of profit and loss under “Salaries and related expenses”.

Deferred taxes

The recognition of deferred tax relates to temporary differences between the Book value of assets and liabilities for financial reporting purposes and their value for tax purposes. However, the Group does not recognize deferred taxes for the following temporary differences:

- Initial recognition of goodwill

- The initial recognition of assets and liabilities in a transaction that is not a business combination and that does affect the accounting income and profit for tax purposes.

- Differences resulting from investments in subsidiaries and companies included on equity basis, if the Group has control when the difference is reversed, and it is expected that they will not be reversed in the foreseeable future, whether by way of realization of the investment or by way of distribution of dividends in respect of the investment.

The measurement of deferred taxes reflects the tax consequences that will result from the way in which the Group expects, at the end of the reporting period, to reinstate or dispose of the book value of assets and liabilities.

Deferred taxes are measured at the tax rates expected to apply to the temporary differences at the date they are realized, based on the laws that have been enacted or substantively enacted by the balance sheet date.

A deferred tax asset for losses carried forward, unutilized tax credits, tax benefits and deductible temporary differences recognized in the books when it is more likely than not that it will be taxable income which can be utilized in the future. Deferred tax assets are reviewed at each reporting date and, if it is not expected that the related tax benefits will be realized, they are reduced.

In order to determine that it is possible to recognize a deferred tax asset, the Group takes into account all the available evidence - both positive evidence supporting the recognition of a deferred tax asset and negative evidence negating recognition as a deferred tax asset.

Offsetting deferred tax assets and liabilities

The Bank offsets deferred tax assets and liabilities if there is a legally enforceable right to offset current tax assets and liabilities, and they are attributable to the same taxable income taxed by the same tax authority in respect of the same entity that is assessed, or various companies in the Group that intend to settle current tax assets and liabilities on a net basis or the tax assets and liabilities are settled simultaneously.

Note 1 – Significant Accounting Policies (cont'd)

Additional tax on the distribution of dividends

The Group may be liable for additional tax in the event of distribution of dividends by Group companies. This additional tax is not included in the financial statements when the Group company policy is not to bring about the distribution of a dividend involving additional tax to the recipient company in the foreseeable future. In cases where the investee company is expected to distribute a dividend involving additional tax for the company, the Group creates a provision for tax in respect of the tax increment that the Group may incur in respect of the dividend distribution.

Additional taxes on income arising from the distribution of dividends by the Bank are charged to profit and loss at the date the liability to pay the related dividend is recognized.

Intercompany transactions

Deferred tax in respect of intercompany transactions in the consolidated accounts is recorded at the rate of tax of the acquiring company.

Uncertain tax positions

The Bank recognizes the effect of tax positions only if it is more likely than not that the positions will be accepted by the tax authorities or the Court. Recognized tax positions are measured at the maximum sum whose probability of realization exceeds 50%. Changes in recognition or measurement are reflected in the period in which changes occur in the circumstances that led to a change in judgment.

T. Earnings per share

The Bank reports basic and diluted earnings per share with regard to its weighted ordinary share capital. Basic earnings per share are calculated by dividing the profit or loss attributed to the ordinary shareholders of the Bank by the weighted average number of ordinary shares that were in circulation during the period. Diluted earnings per share is determined by adjusting the profit or loss relating to the ordinary shareholders, and adjusting the weighted average of ordinary shares in circulation, for the effect of all the potential dilutive ordinary shares.

U. Related party disclosures

IAS 24 – Related Party Disclosures, determines the disclosure requirement an entity has to make of its relationships with a related party and of transactions and unpaid balances with the related party.

In addition, disclosure is to be made of remuneration to key management personnel defined as persons having authority and responsibility for planning the activity of the entity, guiding and controlling it directly or indirectly, including directors.

V. Transactions with controlling owners

The Bank implements US GAAP for the accounting treatment of transactions between a banking corporation and its controlling owner and a company controlled by the Bank. In those situations where the said principles do not refer to the manner of treatment, the Bank implements the principles set out in Standard No. 23 of the Israel Accounting Standards Board on the matter.
Assets and liabilities regarding which a transactions was carried out with a controlling owner are measured for fair value at the date of the transaction. Due to the fact that this is an equity-type transaction, the Group charges the difference between the fair value and the transaction proceeds to equity.

Note 1 – Significant Accounting Policies (cont'd)

W. Impairment in value of non-monetary assets

1. The Bank examines the necessity, for every reporting period, of recording a provision for the impairment of non-monetary assets (such as: buildings and equipment, investments in companies included on equity basis, intangible assets including goodwill) when there are signs, resulting from events or changes in circumstances, which indicate that its assets in the balance sheet are shown at an amount which is in excess of their recoverable value.

The recoverable amount of an asset or a cash-generating unit is the higher of the net selling price and the value-in-use. The value-in-use is the present value of the estimated future cash flows, discounted by the pre-tax rate of interest, which are expected to be derived from use and realization of the asset. For the purpose of examining impairment, assets which cannot be examined individually are grouped together into the smallest group generating cash flows from continued use, which is largely independent of assets in other groups ("cash-generating unit"). For the purpose of examining impairment of goodwill recognized in the framework of a business combination, cash-generating units to which goodwill has been allocated are grouped so that the level at which impairment is examined represents the lowest level at which goodwill can be monitored for purposes of internal reporting, but will not be larger than an operational segment. When there is a change in the composition of one or more cash-generating units to which the goodwill was allocated, the goodwill is to be reallocated to those units affected.

Assets of the head office of the Bank do not produce separate cash flows. If there are indications that impairment has occurred in an asset belonging to the Bank's headquarters, a recoverable value is determined for the group of cash producing units served by the headquarters.

When the value of the asset is higher than its recoverable value, the Bank recognizes a loss from the impairment in value in the amount of the difference between the book value of the asset and its recoverable value. The loss thus recognized will be cancelled only in the event of changes occurring in the estimates that were used to determine the recoverable value of the asset after the date on which the most recent loss from the decline in value was recognized, except for impairment of value of goodwill, which is not cancelled.

2. Impairment with regard to costs of in-house software development

Examination for impairment with regard to costs of in-house software development is to be carried out if the indicators stated in US GAAP exist:

a. It is not expected that the software will provide any significant potential uses;

b. A material change has occurred in the manner or scope of use of the software or of the expected use of the software;

c. A material change has been made or will be made to the software;

d. Costs for developing or adapting the software designated for in-house use deviate significantly from the sums projected in advance;

e. It is no longer expected that the software will be completed and utilized.

If one or more of the indicators stated above exist, it is required to make an examination for impairment in accordance with the principles set out in IAS 36 – Impairment of Assets.

Note 1 – Significant Accounting Policies (cont'd)

3. Impairment of investments in companies included on equity basis reported according to the equity basis method

An investment in a company included on equity basis is examined for impairment when there is objective evidence indicative of impairment in accordance with IAS 39 – Preparation and Measurement of Financial Instruments.

Impairment is examined with relation to the investment as a whole. Goodwill representing part of the investment account in a company included on equity basis is not recognized separately, and is therefore not examined separately in the test for impairment. If there is objective evidence indicative that there may be impairment of the investment, the Group makes an evaluation of the amount refundable of the investment which is the higher of the useful value and its net sale price.

When determining the usage value of an investment in a company included on equity basis, the Group assesses its share in the present value of estimated future cash flows, which are forecast to be generated by the company included on equity basis, including cash flows from activities of the company included on equity basis and the consideration from the final realization of the investment, or the present value of estimated future cash flows that are forecast to stem from dividends received and the final realization.

A loss from impairment is recognized when the book value of the investment, after applying the equity base method, exceeds the recoverable amount, and is recognized under the "share of the banking corporation in operating gains or losses of companies included on equity basis, after taxes" in the profit and loss statement. A loss from impairment is not allocated to any asset, including goodwill comprising part of the investment account in the company included on equity basis. A loss from impairment will be canceled only if changes have taken place in assessments used in determining the recoverable amount of the investment from the date the loss from impairment was last recognized. The book value of the investment, after canceling the loss from impairment, shall not exceed the book value of the investment that would have been determined according to the equity base method if the loss from impairment had not been recognized. Cancelation of the loss from impairment will be recognized under the "share of the corporation in profits of companies included on equity basis, after taxes".

X. New Accounting Standards and Directives of the Supervisor of Banks in the period prior to their implementation

1. Accounting Standard No. 29 – Adoption of International Financial Reporting Standards prescribes that entities that are subject to the Securities Law, 1968, and that are required to report according to the regulations of that law, shall prepare their financial statements in accordance with IFRS for periods commencing 1 January 2008. The aforementioned does not yet apply to banking corporations, the financial statements of which are prepared in accordance with the directives and guidelines of the Supervisor of Banks.

In June 2009, the Banking Supervision Department published a circular on the subject of "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. Pursuant to the circular, the target date for reporting of banking corporations and credit card companies according to IFRS standards is:

Standards on subjects that are a core part of the banking business - the Banking Supervision Department intends to make a final decision that will be made while taking into account the timetable laid down in the U.S., and progress made in the process of convergence between the international and U.S. standards boards.

Note 1 – Significant Accounting Policies (cont'd)

Standards on subjects that are not a core part of the banking business were adopted gradually during 2012 and 2013, except for the subject of employee rights.

2. On 30 January 2014, the Banking Supervision Department published a draft on the adoption of US GAAP regarding employee rights. The draft updates the requirements for recognition, measurement and disclosure, but does not include all the updates required to the directives pursuant to adoption of these rules. These subjects, including further clarifications if necessary, will be dealt with separately.

The draft stipulates that the amendments to the Public Reporting Directives will apply from 1 January 2015, and on initial implementation, a bank will amend retroactively the comparative figures for periods commencing 1 January 2013 and thereafter to comply with the requirements the above rules, inter alia, in accordance with that stated in the draft:

- The discount rate for calculating the liability for employee benefits will be based on market yields of government bonds in Israel. Accordingly, the temporary provision in existing directives fixing the discount rate for calculating the reserves to cover employee benefits will be cancelled.
- Banking corporations will implement GAAP in U.S. banks on the subject of share-based payments as stated in ASC 718 - Compensation - Stock Compensation.

According to the draft published by the Banking Supervision Department, the Bank is required to disclose in its financial statements for 2013 at least an estimate of the quantitative impact on shareholders' equity of the calculation of liabilities for employee rights at the reporting date using discount rates based on market yields of government bonds in Israel. In the Bank's estimation, if the standard had been applied to the Bank at 31 December 2013, in the current interest rate environment, the expected impact on the shareholders' equity of the Bank as at 31 December 2013 in respect of the effect of the change in the discount rate is a decrease in the amount of about NIS 2.3 billion after the effect of tax (about NIS 3.7 billion before tax). Of course, this liability will be updated according to changes in the relevant market interest in the coming years.

It is to be clarified that the adoption of U.S. GAAP on employee benefits may have additional impacts on the Bank's capital which we are studying. One of these possible impacts is the manner of accrual of the liability. From estimates and preliminary interpretations, the effect of the change in the manner of accrual of the liabilities may result in a further decrease in shareholders' equity of NIS 0.25 billion (NIS 0.4 billion before tax). The Bank is examining additional interpretations of the manner of spreading the liabilities and / or additional effects that may alter these estimates.

Despite the significant effect reducing shareholder's equity, for purposes of calculating capital requirements under Basel III directives in accordance with the transitional provisions established in Proper Conduct of Banking Business Directive No. 299, the accumulated balance of profit or loss in respect of re-measurements of net liabilities or net assets for a defined benefit to employees, will not be taken into account immediately but will be subject to transitional provisions over several years.

3. Format of the statement of profit and loss for a banking corporation and adoption of generally accepted accounting principles in U.S. banks on the measurement of interest income

On 29 December 2011, a Supervisor of Banks circular was promulgated intended to adapt the Public Reporting Directives for purposes of adoption of the rules prescribed in accounting standards generally accepted in the US on “Nonrefundable Fees and Other Costs” - the directive establishes rules for commissions from originating loans and direct loan originating costs. Eligible fees and costs according to criteria specified in the directive will not be recognized immediately in the statement of profit and loss, but will be taken into account in calculating the effective interest rate of the loan. In addition, the directive changes the treatment of fees and costs associated with commitments to allocate credit, including credit card transactions. Furthermore, rules were set out in the directive regarding the treatment of changes in the terms of the debt that do not constitute a restructuring of a troubled debt, the treatment of early repayments of debts, and the treatment of other transactions granting credit, such as syndicated transactions.

During the month of October 2013, an FAQ was published on the subject, which sets certain guidelines and clarifications on the manner of implementation of FAS 91. An update was also published of transitional provisions on the measurement of interest income, which sets out guidelines on the manner of first-time implementation. Among other things, it was determined that initial implementation will be made prospectively on transactions originated or renewed after 1 January 2014, and the continued spread of early repayment fees in respect of early repayments made before the date of initial implementation. In addition, it was clarified that a banking corporation cannot defer internal costs in making loans without prior approval from the Financial Reporting Unit in the Banking Supervision Department.

The directive is to be implemented from 1 January 2014 without deferment of direct costs incurred in making the loan. Implementation of the circular is not expected to have any substantial effect on the financial statements.

4. Collective Allowance for Credit Losses

On 18 July 2013, a draft circular to update the Public Reporting Directives on the "Collective Allowance for Credit Losses" was forwarded for discussion to the Advisory Committee. The draft extends the applicability of the temporary provision on the subject of calculating a collective allowance for credit losses and provides comments and guidance for the method of calculation of the rate the allowance, taking into account the adjustments required in respect of environmental factors. In addition, the draft requires significant expansion of the requirements for documentation supporting the rates of allowance and the requirements for reporting to management and the Board of Directors.

The expected impact due to implementation of the guidelines in connection with calculating past loss rates will be dealt with by way of changing the estimate and will be recognized in profit or loss. The initial date of implementation has not yet been finalized. At this stage, the Bank is unable to estimate the effect of adopting the draft once it is implemented.

5. Reporting of amounts reclassified from accumulated other comprehensive income

On 30 September 2013, the Supervisor of Banks issued a circular on reporting amounts reclassified from accumulated other comprehensive income in accordance with US accounting standard update ASU 2013-02. The circular adds a requirement to the Note on accumulated other comprehensive income (loss) to disclose items in the statement of profit and loss to which the amounts were reclassified from accumulated other comprehensive income.

Implementation of the directive will be made retrospectively from 1 January 2014. Implementation of the circular is not expected to have any effect on the financial statements apart from an effect on the presentation of the Note on accumulated other comprehensive income (loss).

6. Bringing forward the date of publication of statements to the public

On 29 September 2013, an instruction was published by the Supervisor of Banks that all banking corporations are to publish their annual financial statements within two months of the year-end (by the end of February) and no later than three months, as required currently by the directives. At the same time, the publication period of quarterly financial statements was shortened from two months to 45 days from the end of the quarter.

Bringing forward the dates of publication is aimed at adapting to usual practice in the U.S., with the necessary adjustments, and in order to improve accessibility to data for the users of the financial statements.

The change will be implemented gradually over three years, until full implementation in 2016.

The Bank, with the agreement of the Banking Supervision Department, postponed implementation of the directive on bringing forward the dates of publication of the financial statements so that the directive will be implemented for the first time only in the financial statements for the first quarter of 2014.

Implementing the directive requires a change in the manner of recording equity profits of a company included on equity basis such that from the first quarter there will be a recurring gap of a quarter between the date of publication of the report of the Bank and of the company included on equity basis.

Note 2 – Cash and deposits with banks

	31 December 2013	31 December 2012
	(NIS millions)	
Cash and deposits with central banks	**35,038**	43,248
Deposits with commercial banks (1)	**9,313**	11,373
Total	**44,351**	54,621
Including: Cash and deposits with central and commercial banks for original periods not exceeding three months	**42,777**	51,644

(1) Net of the allowance for credit losses.

Note: For liens – See Note 14.

Note 3 – Securities

	31 December 2013					31 December 2012				
		Amortized cost (for shares - cost)	Other comprehensive accumulated profit (loss)				Amortized cost (for shares - cost)	Other comprehensive accumulated profit (loss)		
	Book value		Profits	Losses	Fair value (1)	Book value		Profits	Losses	Fair value (1)
	(NIS millions)									
(1) Securities available for sale:										
Bonds -										
Government of Israel	**30,736**	**30,552**	**201**	**(17)**	**30,736**	22,998	22,722	276	-	22,998
Foreign governments	**3,843**	**3,840**	**6**	**(3)**	**3,843**	6,454	6,442	13	(1)	6,454
Financial institutions in Israel	**105**	**100**	**6**	**(1)**	**105**	323	304	21	(2)	323
Financial institutions abroad	**5,280**	**5,213**	**87**	**(20)**	**5,280**	5,281	5,231	128	(78)	5,281
Asset-backed (ABS) or mortgage-backed securities	**7,346**	**7,474**	**34**	**(162)**	**7,346**	5,049	4,993	76	(20)	5,049
Others in Israel	**721**	**683**	**39**	**(1)**	**721**	1,039	1,018	26	(5)	1,039
Others abroad	**2,002**	**1,992**	**28**	**(18)**	**2,002**	1,583	1,550	36	(3)	1,583
	50,033	**49,854**	**401**	**(222)**	**50,033**	42,727	42,260	576	(109)	42,727
Shares and mutual funds (2) (5)	**2,828**	**2,744**	**156**	**(72)**	**2,828**	2,167	1,726	453	(12)	2,167
Total securities available for sale (7)	**52,861**	**52,598**	**557** (3)	**(294)** (3)	**52,861**	44,894	43,986	1,029 (3)	(121) (3)	44,894

See notes on next page.

Note 3 – Securities (cont'd)

	31 December 2013					31 December 2012				
	Book value	Amortized cost (for shares - cost)	Unrealized profits from adjustments to fair value	Unrealized losses from adjustments to fair value	Fair value (1)	Book value	Amortized cost (for shares - cost)	Unrealized profits from adjustments to fair value	Unrealized losses from adjustments to fair value	Fair value (1)
	(NIS millions)									
(2) Securities held for trading:										
Bonds -										
Government of Israel	7,104	7,057	56	(9)	7,104	8,980	8,829	152	(1)	8,980
Foreign governments	1,028	1,036	-	(8)	1,028	311	311	-	-	311
Financial institutions in Israel	327	322	5	-	327	129	127	2	-	129
Financial institutions abroad	116	114	2	-	116	88	88	1	(1)	88
(ABS) or mortgage-backed securities (MBS)	279	282	1	(4)	279	358	358	8	(8)	358
Others in Israel	409	400	9	-	409	707	697	13	(3)	707
Others abroad	520	529	3	(12)	520	742	682	60	-	742
	9,783	9,740	76	(33)	9,783	11,315	11,092	236	(13)	11,315
Shares and mutual funds	1,091	1,017	78	(4)	1,091	199	189	11	(1)	199
Total securities for trading	10,874	10,757	154 (4)	(37) (4)	10,874	11,514	11,281	247 (4)	(14) (4)	11,514
Total securities (6)(7)	63,735	63,355	711	(331)	63,735	56,408	55,267	1,276	(135)	56,408

(1) Fair value data are generally based on stock exchange prices, which do not necessarily reflect the price which will be obtained upon sale of securities in large volumes.
(2) Book value includes NIS 1,363 million with regard to shares and funds which have no readily available fair value, which are shown at cost (31 December 2012 - NIS 1,194 million).
(3) Regarding securities available for sale, other comprehensive income (loss) – unrealized profits (losses) are included in equity in the item "other comprehensive income (loss), net after the effect of tax", except for securities intended as hedging instruments for hedging fair value.
(4) Charged to the profit and loss statement but not yet realized.
(5) During 2013, the Bank realized its holdings in the shares of Migdal Financial and Insurance Holdings Ltd.
(6) Of which: book value of NIS 27 million (31 December 2012 – NIS 93 million) in respect of bonds of companies included on equity basis.
(7) Including impaired bonds in the amount of NIS 26 million (31 December 2012 – NIS 101 million).

General comments:
Securities lent amounting to NIS 696 million (31 December 2012 – NIS 339 million) are shown under credit to the public.
Securities pledged to lenders amounted to NIS 1,458 million (31 December 2012 – NIS 1,851 million).

For liens – see Note 14.
For details of results of investment activities in bonds and in shares and mutual funds – see Notes 20 and 21.
The distinction between Israeli and foreign bonds is made in accordance with the country of residence of the entity issuing the security, as stated in Exhibit G in the Management Review on "Foreign Country Exposure".

Note 3 – Securities (cont'd)

Additional details on consolidated basis of mortgage-backed and asset-backed securities available for sale

	31 December 2013				
			Other comprehensive accumulated profit (loss) (1)		
	Book value	Amortized cost	Profits	Losses	Fair value
	(NIS millions)				
(3) Bonds available for sale					
Pass-through securities:					
Securities guaranteed by GNMA	232	233	1	(2)	232
Securities issued by FNMA and FHLMC	1,581	1,662	-	(81)	1,581
Total	1,813	1,895	1	(83)	1,813
Other mortgage-backed securities (including CMO and STRIPPED MBS)					
Securities issued by FNMA, FHLMC, or GNMA, or guaranteed by these entities	3,363	3,423	6	(66)	3,363
Other mortgage-backed securities	355	355	-	-	355
Total	3,718	3,778	6	(66)	3,718
Asset-backed securities (ABS)					
Credit card receivables	85	86	-	(1)	85
Lines of credit for any purpose secured by dwelling	2	2	-	-	2
Other credit to private persons	3	3	-	-	3
Other credit not to private persons	1	1	-	-	1
CLO debentures	1,724	1,709	27	(12)	1,724
Total	1,815	1,801	27	(13)	1,815
Total asset-backed bonds available for sale	7,346	7,474	34	(162)	7,346

(1) Amounts charged to capital reserve as part of other comprehensive income, net after the effect of tax.

Note 3 – Securities (cont'd)

Additional details of mortgage-backed and asset-backed securities available for sale (cont'd)

	31 December 2012				
			Other comprehensive accumulated profit (loss) (1)		
	Book value	Amortized cost	Profits	Losses	Fair value
	(NIS millions)				
(3) Bonds available for sale					
Pass-through securities:					
Securities guaranteed by GNMA	257	257	1	(1)	257
Securities issued by FNMA and FHLMC	511	510	1	-	511
Total	768	767	2	(1)	768
Other mortgage-backed securities (including CMO and STRIPPED MBS)					
Securities issued by FNMA, FHLMC, or GNMA, or guaranteed by these entities	2,560	2,544	16	-	2,560
Other mortgage-backed securities	303	300	4	(1)	303
Total	2,863	2,844	20	(1)	2,863
Asset-backed securities (ABS)					
Credit card receivables	38	38	-	-	38
Lines of credit for any purpose secured by dwelling	2	2	-	-	2
Other credit to private persons	4	4	-	-	4
CLO debentures	1,371	1,334	54	(17)	1,371
Others	3	4	-	(1)	3
Total	1,418	1,382	54	(18)	1,418
Total asset-backed bonds available for sale	5,049	4,993	76	(20)	5,049

(1) Amounts charged to capital reserve as part of other comprehensive income, net after the effect of tax.

Note 3 – Securities (cont'd)

Additional details on consolidated basis of mortgage-backed and asset-backed securities for trading

	31 December 2013				
	Book value	Amortized cost	Unrealized profits from adjustments to fair value[1]	Unrealized losses from adjustments to fair value[1]	Fair value
	(NIS millions)				
(4) Debentures for trading					
Pass-through securities					
Other securities	4	4	-	-	4
Total	4	4	-	-	4
Other mortgage-backed securities (including CMO and STRIPPED MBS)					
Securities issued by FNMA, FHLMC, or GNMA, or guaranteed by these entities	11	11	-	-	11
Other mortgage-backed securities	73	76	-	(3)	73
Total	84	87	-	(3)	84
Asset-backed securities (ABS)					
Credit card receivables	-	-	-	-	-
Lines of credit for any purpose secured by dwelling	-	-	-	-	-
Credit for purchase of vehicles	57	56	1	-	57
Other credit to private persons	16	16	-	-	16
Credit not to private persons	-	-	-	-	-
CDO debentures	-	-	-	-	-
Others	118	119	-	(1)	118
Total	191	191	1	(1)	191
Total asset-backed debentures for trading	279	282	1	(4)	279

(1) These profits (losses) have been charged to profit and loss.

Note 3 – Securities (cont'd)

Additional details of mortgage-backed and asset-backed securities for trading (cont'd)

	31 December 2012				
	Book value	Amortized cost	Unrealized profits from adjustments to fair value[1]	Unrealized losses from adjustments to fair value[1]	Fair value
	(NIS millions)				
(4) Debentures for trading (cont'd)					
Pass-through securities					
Other securities	5	5	-	-	5
Total	5	5	-	-	5
Other mortgage-backed securities (including CMO and STRIPPED MBS)					
Securities issued by FNMA, FHLMC, or GNMA, or guaranteed by these entities	21	19	2	-	21
Other mortgage-backed securities	19	21	-	(2)	19
Total	40	40	2	(2)	40
Asset-backed securities (ABS)					
Credit card receivables	37	37	-	-	37
Lines of credit for any purpose secured by dwelling	3	2	1	-	3
Credit for purchase of vehicles	166	163	3	-	166
Other credit to private persons	16	16	-	-	16
Credit not to private persons	1	1	-	-	1
CDO debentures	28	33	-	(5)	28
Others	62	61	2	(1)	62
Total	313	313	6	(6)	313
Total asset-backed securities for trading	358	358	8	(8)	358

(1) These profits (losses) have been charged to profit and loss.

Note 3 – Securities (cont'd)

Additional details of fair value and unrealized losses by period and rate of impairment of securities available for sale and held for trading that are in an unrealized loss position

	31 December 2013									
	Less than 12 months					12 months and above				
		Unrealized losses					Unrealized losses			
	Fair value	0-20%	20%-35%	More than 35%	Total	Fair value	0-20%	20%-35%	More than 35%	Total
	(NIS millions)									
Bonds										
Government of Israel	408	16	-	-	16	28	-	-	-	-
Foreign governments	1,032	2	-	-	2	45	1	-	-	1
Financial institutions in Israel	-	-	-	-	-	9	1	-	-	1
Financial institutions abroad	1,394	6	-	-	6	539	10	4	-	14
Asset-backed securities (ABS) or mortgage-backed securities (MBS)	4,495	130	-	-	130	779	32	-	-	32
Others in Israel	9	1	-	-	1	66	-	-	-	-
Others abroad	601	13	-	-	13	351	5	-	-	5
Shares	966	72	-	1	73	-	-	-	-	-
Total securities available for sale	8,905	240	-	1	241	1,817	49	4	-	53

	31 December 2012									
	Less than 12 months					12 months and above				
		Unrealized losses					Unrealized losses			
	Fair value	0-20%	20%-35%	More than 35%	Total	Fair value	0-20%	20%-35%	More than 35%	Total
	(NIS millions)									
Bonds										
Government of Israel	302	-	-	-	-	-	-	-	-	-
Foreign governments	1,032	3	-	-	3	9	1	-	-	1
Financial institutions in Israel	-	-	-	-	-	28	-	2	-	2
Financial institutions abroad	335	2	-	-	2	1,727	69	4	-	73
Asset-backed securities (ABS) or mortgage-backed securities (MBS)	876	4	-	-	4	386	16	-	-	16
Others in Israel	7	-	-	-	-	198	5	-	-	5
Others abroad	195	1	-	-	1	169	2	-	-	2
Shares	12	9	-	3	12	-	-	-	-	-
Total securities available for sale	2,759	19	-	3	22	2,517	93	6	-	99

Note 3 – Securities (cont'd)

Additional details of mortgage-backed and asset-backed securities that are in an unrealized loss position

	31 December 2013					
	Less than 12 months		More than 12 months		Total	
	Fair value	Unrealized losses from adjustments to fair value	Fair value	Unrealized losses from adjustments to fair value	Fair value	Unrealized losses from adjustments to fair value
	(NIS millions)					
Mortgage-backed securities (MBS)	**1,362**	**(66)**	**315**	**(17)**	**1,677**	**(83)**
Other mortgage-backed securities (including REMIC, CMO and STRIPPED MBS)	**2,435**	**(56)**	**289**	**(10)**	**2,724**	**(66)**
Asset-backed securities (ABS)	**698**	**(8)**	**175**	**(5)**	**873**	**(13)**
Total	**4,495**	**(130)**	**779**	**(32)**	**5,274**	**(162)**

	31 December 2012					
	Less than 12 months		More than 12 months		Total	
	Fair value	Unrealized losses from adjustments to fair value	Fair value	Unrealized losses from adjustments to fair value	Fair value	Unrealized losses from adjustments to fair value
	(NIS millions)					
Mortgage-backed securities (MBS)	351	(1)	-	-	351	(1)
Other mortgage-backed securities (including REMIC, CMO and STRIPPED MBS)	457	(1)	12	-	469	(1)
Asset-backed securities (ABS)	70	(2)	372	(16)	442	(18)
Total	878	(4)	384	(16)	1,262	(20)

Note 3 – Securities (cont'd)

Mortgage Backed Security – MBS
Debentures backed by mortgages for which the payments of interest and principal are based on cash flows resulting from the repayment of loans secured by mortgages.

Sub-Prime – a particular type of MBS
Debentures for which the interest and principal payments are based on a cash flow from portfolios of mortgages given to borrowers with low credit ratings who are not able to provide appropriate collateral.

Collateralized Debt Obligation - CDO
A debenture backed by a portfolio of debentures and/or loans with varying levels of seniority and ratings.

Synthetic Collateralized Debt Obligation – SCDO
An agreement backed by a portfolio of CDS (which are tranches) with varying levels of seniority.

Collateralized Loan Obligation – CLO
A debenture backed by a portfolio of loans.

Federal National Mortgage Association - FNMA ("Fannie Mae")
A public company backed by the United States government which purchases mortgages, securitizes them and sells them on the open market (this company's securities do not have U.S. government guarantees).

Federal Home Loan Mortgage Corporation - FHLMC ("Freddie Mac")
A United States government sponsored enterprise which purchases mortgages, securitizes them and sells them on the open market (this company's securities do not have U.S. government guarantees).

Government National Mortgage Association - GNMA ("Ginnie Mae")
A federal mortgage company. Bonds issued by it are guaranteed by the Government National Mortgage Association.

Credit Default Swap – CDS
A financial instrument which transfers the issuer's credit exposure between parties to the transaction.

Note 4 – Credit Risk, Credit to the Public and the Allowance for Credit Losses

A. Debts[1] and off-balance sheet credit instruments
Allowance for credit losses

1. Change in balance of credit loss allowance

	31 December 2013					
	Allowance for credit losses					
	Credit to the public				Banks and	
	Commercial	Residential	Other private	Total	governments	Total
	(NIS millions)					
Balance of allowance for credit losses at beginning of year	**3,691**	**475**	**395**	**4,561**	**4**	**4,565**
Expenses in respect of credit losses	**30**	**53**	**182**	**265**	**3**	**268**
Accounting write-offs	**(485)**	**(29)**	**(451)**	**(965)**	**(5)**	**(970)**
Collection of debts written off in previous years	**80**	**-**	**371**	**451**	**-**	**451**
Net accounting write-offs	**(405)**	**(29)**	**(80)**	**(514)**	**(5)**	**(519)**
Translation differences reserve	**(15)**	**(1)**	**(1)**	**(17)**	**-**	**(17)**
Balance of allowance for credit losses at end of year[2]	**3,301**	**498**	**496**	**4,295**	**2**	**4,297**
[2]Of which: in respect of off-balance sheet credit instruments	**373**	**-**	**39**	**412**	**-**	**412**

	31 December 2012					
	Allowance for credit losses					
	Credit to the public				Banks and	
	Commercial	Residential	Other private	Total	governments	Total
	(NIS millions)					
Balance of allowance for credit losses at beginning of year	3,441	532	462	4,435	5	4,440
Other changes in the allowance for credit losses at 1 January 2012	27	3	6	36	-	36
Expenses in respect of credit losses	1,156	(13)	93	1,236	-	1,236
Accounting write-offs	(1,084)	(47)	(430)	(1,561)	(1)	(1,562)
Collection of debts written off in previous years	155	-	264	419	-	419
Net accounting write-offs	(929)	(47)	(166)	(1,142)	(1)	(1,143)
Adjustments from translation of financial statements	(4)	-	-	(4)	-	(4)
Balance of allowance for credit losses at end of year[2]	3,691	475	395	4,561	4	4,565
[2]Of which: in respect of off-balance sheet credit instruments	413	-	34	447	-	447

(1) Credit to the public, credit to governments, deposits in banks (in 2013, excluding deposits in the Bank of Israel) and other debts, excluding bonds and securities borrowed or purchased under agreements to resell.

Note 4 – Credit Risk, Credit to the Public and the Allowance for Credit Losses

A. Debts[1] and off-balance sheet credit instruments
Allowance for credit losses

1. Change in balance of credit loss allowance (cont'd)

	31 December 2011					
	Credit loss allowance					
	Credit to the public				Banks and	
	Commercial	Residential	Other private	Total	governments	Total
	(NIS millions)					
Balance of credit loss allowance at beginning of year	8,394	487	1,659	10,540	1	10,541
Net accounting write-offs recognized at 1.1.2011	(4,371)	-	(1,469)	(5,840)	-	(5,840)
Other changes in the credit loss allowance at 1 January 2011 (charged to equity)	530	123	421	1,074	-	1,074
Balance of allowance at 1.1.2011	4,553	610	611	5,774	1	5,775
Expenses in respect of credit losses	729	(9)	10	730	4	734
Accounting write-offs	(1,917)	(69)	(532)	(2,518)	-	(2,518)
Collection of debts written off in previous years	76	-	373	449	-	449
Net accounting write-offs	(1,841)	(69)	(159)	(2,069)	-	(2,069)
Balance of credit loss allowance at end of year	3,441	532	462	4,435	5	4,440
Of which: in respect of off-balance sheet credit instruments	429	-	35	464	-	464

(1) Credit to the public, credit to governments, deposits in banks (in 2013, excluding deposits in the Bank of Israel) and other debts, excluding bonds and securities borrowed or purchased under agreements to resell.

Note 4 – Credit Risk, Credit to the Public and the Allowance for Credit Losses (cont'd)

A. Debts[1] and off-balance sheet credit instruments (cont'd)

2. Additional information on the method of calculating the credit loss allowance in respect of debts[1] and on the debts[1] on which it was calculated

	31 December 2013					
	Allowance for credit losses					
	Credit to the public				Banks and governments	Total
	Commercial	Residential	Other private	Total		
	(NIS millions)					
Recorded debt balance of debts[1]:						
Examined on an individual basis	**109,908**	**49**	**1,709**	**111,666**	**12,809**	**124,475**
Examined on a collective basis[4]	**32,564**	**69,741**	**30,786**	**133,091**	**2,453**	**135,544**
[4]Of which: the allowance was calculated by extent of arrears	**-**	**68,581**	**-**	**68,581**	**-**	**68,581**
Total debts*	**142,472**	**69,790**	**32,495**	**244,757**	**15,262**	**260,019**
Allowance for credit losses in respect of debts[1]:	**-**	**-**	**-**	**-**	**-**	**-**
Examined on an individual basis	**2,660**	**15**	**87**	**2,762**	**2**	**2,764**
Examined on a collective basis[5]	**268**	**483**	**370**	**1,121**	**-**	**1,121**
[5]Of which: the allowance was calculated by extent of arrears	**-**	**480**	**-**	**480**	**-**	**480**
Total allowance for credit losses	**2,928**	**498**	**457**	**3,883**	**2**	**3,885**

	31 December 2012					
	Allowance for credit losses					
	Credit to the public				Banks and governments	Total
	Commercial	Residential	Other private	Total		
	(NIS millions)					
Recorded debt balance of debts[1]:						
Examined on an individual basis	120,006	48	1,991	122,045	45,770	167,815
Examined on a collective basis[4]	31,634	63,355	28,344	123,333	7,158	130,491
[4]Of which: the allowance was calculated by extent of arrears	-	62,423 (3)	-	62,423	-	62,423
Total debts[1]	151,640	63,403	30,335	245,378	52,928	298,306
Allowance for credit losses in respect of debts[1]:	-	-	-	-	-	-
Examined on an individual basis	2,943	19	62	3,024	4	3,028
Examined on a collective basis[5]	335	456	299	1,090	-	1,090
[5]Of which: the allowance was calculated by extent of arrears	-	450 (3)	-	450	-	450
Total allowance for credit losses	3,278	475	361	4,114	4	4,118

(1) Credit to the public, credit to governments, deposits in banks (in 2013, excluding deposits in the Bank of Israel) and other debts, excluding bonds and securities borrowed or purchased under agreements to resell.
(2) Reclassified
(3) Including balance of allowance in excess of that required by the extent of arrears method calculated on a collective basis in the amount of NIS 271 million (2012 – NIS 209 million).

Note 4 – Credit Risk, Credit to the Public and the Allowance for Credit Losses (cont'd)

B. Debts[1]

1. Credit quality and arrears

	31 December 2013					
		Problem debts(2)			Unimpaired debts - additional information	
	Non-problem debts	Not impaired	Impaired(3)	Total	In arrears of 90 days or more(4)	In arrears of 30 to 89 days(5)
	(NIS millions)					
Activity of borrowers in Israel						
Public - commercial						
Construction & real estate - construction	13,684	558	478	14,720	6	15
Construction & real estate - real estate activities	21,786	196	1,392	23,374	5	21
Financial services	10,472	319	345	11,136	156	10
Commercial - other	61,866	2,364	1,769	65,999	31	83
Total commercial	107,808	3,437	3,984	115,229	198	129
Private individuals - housing loans(6)	67,789	803	-	68,592	786	602
Private individuals - other	31,046	306	106	31,458	112	196
Total public - activity in Israel	206,643	4,546	4,090	215,279	1,096	927
Israeli banks	1,688	-	-	1,688	-	-
Government of Israel	338	-	-	338	-	-
Total activity in Israel	208,669	4,546	4,090	217,305	1,096	927
Activity of borrowers abroad						
Public - commercial						
Construction & real estate	6,783	166	718	7,667	34	122
Other commercial	18,389	317	870	19,576	258	72
Total commercial	25,172	483	1,588	27,243	292	194
Private individuals	2,126	19	90	2,235	52	30
Total public - activity abroad	27,298	502	1,678	29,478	344	224
Foreign banks	13,016	-	-	13,016	-	-
Foreign governments	220	-	-	220	-	-
Total activity abroad	40,534	502	1,678	42,714	344	224
Total public	233,941	5,048	5,768	244,757	1,440	1,151
Total banks	14,704	-	-	14,704	-	-
Total governments	558	-	-	558	-	-
Total	249,203	5,048	5,768	260,019	1,440	1,151

See notes below.

Note 4 – Credit Risk, Credit to the Public and the Allowance for Credit Losses (cont'd)

B. Debts[1] (cont'd)

1. Credit quality and arrears (cont'd)

	31 December 2012					
		Problem debts(2)			Unimpaired debts - additional information	
	Non-problem debts	Not impaired(7)	Impaired(3)	Total	In arrears of 90 days or more(4)	In arrears of 30 to 89 days(5)
	(NIS millions)					
Activity of borrowers in Israel						
Public - commercial						
Construction & real estate - construction	13,426	168	667	14,261	6	37
Construction & real estate - real estate activities	23,409	285	1,847	25,541	1	26
Financial services	12,105	396	716	13,217	-	17
Commercial - other	62,481	2,359	2,369	67,209	32	100
Total commercial	111,421	3,208	5,599	120,228	39	180
Private individuals - housing loans(6)(7)	61,242	859	-	62,101	829	593
Private individuals - other	28,593	303	45	28,941	115	174
Total public - activity in Israel	201,256	4,370	5,644	211,270	983	947
Israeli banks	38,478	-	-	38,478	-	-
Government of Israel	282	-	-	282	-	-
Total activity in Israel	240,016	4,370	5,644	250,030	983	947
Activity of borrowers abroad						
Public - commercial						
Construction & real estate	7,296	205	874	8,375	76	68
Other commercial	22,087	164	786	23,037	68	159
Total commercial	29,383	369	1,660	31,412	144	227
Private individuals	2,597	5	94	2,696	167	28
Total public - activity abroad	31,980	374	1,754	34,108	311	255
Foreign banks	14,003	-	5	14,008	-	-
Foreign governments	160	-	-	160	-	-
Total activity abroad	46,143	374	1,759	48,276	311	255
Total public	233,236	4,744	7,398	245,378	1,294	1,202
Total banks	52,481	-	5	52,486	-	-
Total governments	442	-	-	442	-	-
Total	286,159	4,744	7,403	298,306	1,294	1,202

B. Debts[1] (cont'd)

1. Credit quality and arrears (cont'd)

Notes:

(1) Credit to the public, credit to governments, deposits in banks (in 2013, excluding deposits in the Bank of Israel) and other debts, excluding bonds and securities borrowed or purchased under agreements to resell.

(2) Impaired, substandard or special mention credit risk, including in respect of housing loans for which there is a provision by extent of arrears, and housing loans fior which there is no provision that are in arrears of 90 days or more.

(3) As a rule, impaired debts do not accrue interest income. For information on certain impaired debts under troubled debt restructuring, see Note 4.B.2.C.

(4) Classified as problem debts that are not impaired, accruing interest income.

(5) Accruing interest income. Debts in arrears of 30 to 89 days in the amount of NIS 165 million were classified as problem debts that are not impaired.

(6) Including housing loans in the amount of NIS 198 million (31 December 2012 – NIS 230 million) with a provision by extent of arrears, in which an arrangement was signed for the repayment of arrears by the borrower, with a change made to the repayment schedule in respect of the loan balance of which the repayment date has not yet arrived.

(7) Reclassified.

Credit quality – status of debts in arrears[1]

The status of debts in arrears is monitored routinely, and serves as one of the key indicators of credit quality. The status of debts in arrears is determined based on actual days of arrears. Debts are treated as nonperforming (not accruing interest income) after 90 days of arrears, as is any debt that has undergone troubled debt restructuring and has resumed accruing interest when it is one day of arrears relative to the new terms of the debt. With regard to debts evaluated on a collective basis, the status of arrears affects the classification of the debt (the classification is more severe for more extensive arrears) and after 150 days of arrears, the Bank performs a charge-off of the debt. With regard to housing loans, with the exception of loans without quarterly or monthly payments, the Bank establishes an allowance according to the method of the extent of arrears.

Note 4 – Credit Risk, Credit to the Public and the Allowance for Credit Losses (cont'd)

B. Debts[1] (cont'd)

2. Additional information on impaired debts
A. Impaired debts and individual allowance

	31 December 2013				
	Balance[2] of impaired debts in respect of which there is an individual allowance[3]	Balance of individual allowance[3]	Balance[2] of impaired debts in respect of which there is no individual allowance[3]	Total balance[2] of impaired debts	Principal contractual balance of impaired debts
	(NIS millions)				
Activity of borrowers in Israel					
Public - commercial					
Construction & real estate - construction	108	23	370	478	1,651
Construction & real estate - real estate activities	979	176	413	1,392	2,520
Financial services	302	143	43	345	1,015
Commercial - other	861	356	908	1,769	5,144
Total commercial	2,250	698	1,734	3,984	10,330
Private individuals - housing loans	-	-	-	-	-
Private individuals - other	67	44	39	106	1,793
Total public - activity in Israel	2,317	742	1,773	4,090	12,123
Israeli banks	-	-	-	-	-
Government of Israel	-	-	-	-	-
Total activity in Israel	2,317	742	1,773	4,090	12,123
Activity of borrowers abroad					
Public - commercial					
Construction & real estate	503	302	215	718	900
Other commercial	695	384	175	870	1,058
Total commercial	1,198	686	390	1,588	1,958
Private individuals	62	49	28	90	105
Total public - activity abroad	1,260	735	418	1,678	2,063
Foreign banks	-	-	-	-	-
Foreign governments	-	-	-	-	-
Total activity abroad	1,260	735	418	1,678	2,063
Total public	3,577	1,477	2,191	5,768	14,186
Total banks	-	-	-	-	-
Total governments	-	-	-	-	-
Total	3,577	1,477	2,191	5,768	14,186
Of which:					
Measured by present value of cash flows	2,203	1,147	1,115	3,318	
Debts under troubled debt restructuring	1,218	348	1,251	2,469	

See notes on next page.

Note 4 – Credit Risk, Credit to the Public and the Allowance for Credit Losses (cont'd)

B. Debts[1] (cont'd)

2. Additional information on impaired debts (cont'd)
A. Impaired debts and individual allowance (cont'd)

	31 December 2012				
	Balance[2] of impaired debts in respect of which there is an individual allowance[3]	Balance of individual allowance[3]	Balance[2] of impaired debts in respect of which there is no individual allowance[3]	Total balance[2] of impaired debts	Principal contractual balance of impaired debts
	(NIS millions)				
Activity of borrowers in Israel					
Public - commercial					
Construction & real estate - construction	79	22	588	667	1,910
Construction & real estate - real estate activities	1,406	187	441	1,847	3,125
Financial services	663	422	53	716	1,196
Commercial - other	1,398	584	971	2,369	5,773
Total commercial	3,546	1,215	2,053	5,599	12,004
Private individuals - housing loans[3]	-	-	-	-	-
Private individuals - other[3]	22	22	23	45	1,681
Total public - activity in Israel	3,568	1,237	2,076	5,644	13,685
Israeli banks	-	-	-	-	-
Government of Israel	-	-	-	-	-
Total activity in Israel	3,568	1,237	2,076	5,644	13,685
Activity of borrowers abroad					
Public - commercial					
Construction & real estate	537	238	337	874	1,101
Other commercial	558	284	228	786	920
Total commercial	1,095	522	565	1,660	2,021
Private individuals	78	52	16	94	96
Total public - activity abroad	1,173	574	581	1,754	2,117
Foreign banks	-	-	5	5	6
Foreign governments	-	-	-	-	-
Total activity abroad	1,173	574	586	1,759	2,123
Total public	4,741	1,811	2,657	7,398	15,802
Total banks	-	-	5	5	6
Total governments	-	-	-	-	-
Total	4,741	1,811	2,662	7,403	15,808
Of which:					
Measured by present value of cash flows	3,257	1,452	1,778	5,035	
Debts under troubled debt restructuring (4)	1,323	188	771	2,094	

(1) Credit to the public, credit to governments, deposits in banks (in 2013, excluding deposits in the Bank of Israel) and other debts, excluding bonds and securities borrowed or purchased under agreements to resell.

(2) Balance of recorded debt.

(3) Individual allowance for credit losses.

(4) Reclassified.

Note 4 – Credit Risk, Credit to the Public and the Allowance for Credit Losses (cont'd)

B. Debts[1] (cont'd)

2. Additional information on impaired debts (cont'd)
B. Average balance and interest income

	31 December 2013		
	Average balance of impaired debts[2]	Interest income recorded[3]	Of which: recorded on cash basis
	(NIS millions)		
Activity of borrowers in Israel			
Public - commercial			
Construction & real estate - construction	549	12	12
Construction & real estate - real estate activities	1,585	19	19
Financial services	513	-	-
Commercial - other	2,028	19	17
Total commercial	4,675	50	48
Private individuals - housing loans	-	-	-
Private individuals - other	68	5	5
Total public - activity in Israel	4,743	55	53
Israeli banks	-	-	-
Government of Israel	-	-	-
Total activity in Israel	4,743	55	53
Activity of borrowers abroad			
Public - commercial			
Construction & real estate	787	8	4
Other commercial	894	16	15
Total commercial	1,681	24	19
Private individuals	92	1	1
Total public - activity abroad	1,773	25	20
Foreign banks	2	-	-
Foreign governments	-	-	-
Total activity abroad	1,775	25	20
Total public	6,516	80	73
Total banks	2	-	-
Total governments	-	-	-
Total	6,518	80 (4)	73

See notes on next page.

Note 4 – Credit Risk, Credit to the Public and the Allowance for Credit Losses (cont'd)

B. Debts[1] (cont'd)

2. Additional information on impaired debts (cont'd)
B. Average balance and interest income (cont'd)

	31 December 2012 (5)	31 December 2011 (5)
	(NIS millions)	
Average recorded debt balance of impaired debts in the reporting period	7,255 (6)	6,764
Total interest income recorded in the reporting period in respect of these debts in the period when they were classified as impaired	62	13
Total interest income that would heve been recorded in the reporting period if these debts accrue interest under their original terms	616	611
Of which: interest income recorded under the cash basis accounting method	53	12

(1) Credit to the public, credit to governments, deposits in banks (in 2013, excluding deposits in the Bank of Israel) and other debts, excluding bonds and securities borrowed or purchased under agreements to resell.
(2) Average debt balance recorded of impaired debts in the reporting period.
(3) Interest income recorded in the reporting period in respect of the average balance of impaired debts, for the period in which the debts were classified as impaired.
(4) If the impaired debts had accrued interest under their original terms, interest income would have been recorded in the amount of NIS 510 million.
(5) In accordance with the directives of the Banking Supervision Department on updating the disclosure of the credit quality of debts and the allowance for credit losses, disclosures are to be included prospectively on troubled debt restructuring as of the financial statements for 31 March 2013. See also Note 1.
(6) Reclassified.

Note 4 – Credit Risk, Credit to the Public and the Allowance for Credit Losses (cont'd)

B. Debts[1] (cont'd)

2. Additional information on impaired debts (cont'd)
C. Impaired debts under restructuring

	31 December 2013				
	Not accruing interest income	Accruing[2] in arrears of 90 days or more	Accruing[2] in arrears of 30 to 89 days	Accruing[2] not in arrears	Total[3]
	(NIS millions)				
Activity of borrowers in Israel					
Public - commercial					
Construction & real estate - construction	301	-	-	-	301
Construction & real estate - real estate activities	607	-	-	-	607
Financial services	48	-	-	-	48
Commercial - other	457	-	-	36	493
Total commercial	1,413	-	-	36	1,449
Private individuals - housing loans (4)	-	-	-	-	-
Private individuals - other (4)	49	-	-	1	50
Total public - activity in Israel	1,462	-	-	37	1,499
Israeli banks	-	-	-	-	-
Government of Israel	-	-	-	-	-
Total activity in Israel	1,462	-	-	37	1,499
Activity of borrowers abroad					
Public - commercial					
Construction & real estate	222	-	-	304	526
Other commercial	201	-	-	203	404
Total commercial	423	-	-	507	930
Private individuals	30	-	-	10	40
Total public - activity abroad	453	-	-	517	970
Foreign banks	-	-	-	-	-
Foreign governments	-	-	-	-	-
Total activity abroad	453	-	-	517	970
Total public	1,915	-	-	554	2,469
Total banks	-	-	-	-	-
Total governments	-	-	-	-	-
Total	1,915	-	-	554	2,469

See notes on next page.

Note 4 – Credit Risk, Credit to the Public and the Allowance for Credit Losses (cont'd)

B. Debts[1] (cont'd)

2. Additional information on impaired debts (cont'd)
C. Impaired debts under restructuring (cont'd)

	31 December 2012				
	Not accruing interest income	Accruing[2] in arrears of 90 days or more	Accruing[2] in arrears of 30 to 89 days	Accruing[2] not in arrears	Total[3]
	(NIS millions)				
Activity of borrowers in Israel					
Public - commercial					
Construction & real estate - construction	114	-	-	-	114
Construction & real estate - real estate activities	782	-	-	38	820
Financial services	93	-	-	-	93
Commercial - other	256	-	-	30	286
Total commercial	1,245	-	-	68	1,313
Private individuals - housing loans (4)	-	-	-	-	-
Private individuals - other (4)	24	-	-	3	27
Total public - activity in Israel	1,269	-	-	71	1,340
Israeli banks	-	-	-	-	-
Government of Israel	-	-	-	-	-
Total activity in Israel	1,269	-	-	71	1,340
Activity of borrowers abroad (4)					
Public - commercial					
Construction & real estate	132	-	-	341	473
Other commercial	68	-	-	186	254
Total commercial	200	-	-	527	727
Private individuals	11	-	-	12	23
Total public - activity abroad	211	-	-	539	750
Foreign banks	-	-	-	4	4
Foreign governments	-	-	-	-	-
Total activity abroad	211	-	-	543	754
Total public	1,480	-	-	610	2,090
Total banks	-	-	-	4	4
Total governments	-	-	-	-	-
Total	1,480	-	-	614	2,094

(1) Credit to the public, credit to governments, deposits in banks (in 2013, excluding deposits in the Bank of Israel) and other debts, excluding bonds and securities borrowed or purchased under agreements to resell.
(2) Accruing interest income.
(3) Included in impaired debts.
(4) Reclassified.

Note 4 – Credit Risk, Credit to the Public and the Allowance for Credit Losses (cont'd)

B. Debts[1] (cont'd)

2. Additional information on impaired debts (cont'd)
C. Impaired debts under restructuring (cont'd)

1. Restructurings carried out

	31 December 2013		
	Number of contracts	Recorded debt balance before restructuring	Recorded debt balance after restructuring
	(NIS millions)		
Activity of borrowers in Israel			
Public - commercial			
Construction & real estate - construction	17	35	23
Construction & real estate - real estate activities	15	165	138
Financial services	-	-	-
Commercial - other	75	5	5
Total commercial	107	205	166
Private individuals - housing loans	-	-	-
Private individuals - other	753	7	7
Total public - activity in Israel	860	212	173
Israeli banks	-	-	-
Government of Israel	-	-	-
Total activity in Israel	860	212	173
Activity of borrowers abroad			
Public - commercial			
Construction & real estate	12	166	166
Other commercial	63	322	321
Total commercial	75	488	487
Private individuals	52	7	7
Total public - activity abroad	127	495	494
Foreign banks	-	-	-
Foreign governments	-	-	-
Total activity abroad	127	495	494
Total public	987	707	667
Total banks	-	-	-
Total governments	-	-	-
Total	987	707	667

(1) Credit to the public, credit to governments, deposits in banks (in 2013, excluding deposits in the Bank of Israel) and other debts, excluding bonds and securities borrowed or purchased under agreements to resell.

(2) In accordance with the directives of the Banking Supervision Department on updating the disclosure of the credit quality of debts and the allowance for credit losses, disclosures are to be included prospectively on troubled debt restructuring as of the financial statements for 31 March 2013. See also Note 1.

Note 4 – Credit Risk, Credit to the Public and the Allowance for Credit Losses (cont'd)

B. Debts[1] (cont'd)

2. Additional information on impaired debts (cont'd)

C. Impaired debts under restructuring (cont'd)

2. Failed restructurings[2]

	31 December 2013	
	Number of contracts	Recorded debt balance
	(NIS millions)	
Activity of borrowers in Israel		
Public - commercial		
Construction & real estate - construction	46	14
Construction & real estate - real estate activities	17	21
Financial services	2	-
Commercial - other	91	55
Total commercial	156	90
Private individuals - housing loans	-	-
Private individuals - other	523	11
Total public - activity in Israel	679	101
Israeli banks	-	-
Government of Israel	-	-
Total activity in Israel	679	101
Activity of borrowers abroad		
Public - commercial		
Construction & real estate	4	8
Other commercial	27	90
Total commercial	31	98
Private individuals	16	3
Total public - activity abroad	47	101
Foreign banks	-	-
Foreign governments	-	-
Total activity abroad	47	101
Total	726	202

(1) Credit to the public, credit to governments, deposits in banks (in 2013, excluding deposits in the Bank of Israel) and other debts, excluding bonds and securities borrowed or purchased under agreements to resell.
(2) Debts that during the reporting year went into arrears of 30 days or more and underwent a troubled debt restructuring during the 12 months preceding the date they became debts in arrears.
(3) Recorded balance of debt at the end of the quarter in which the failure took place.

Note 4 – Credit Risk, Credit to the Public and the Allowance for Credit Losses (cont'd)

B. Debts[1] (cont'd)

3. Additional information on housing loans
Year-end balances by LTV[2], type of repayment and type of interest

		31 December 2013			
		Total[2]	Of which: bullet[2] and balloon	Of which: variable interest[2]	Total off-balance sheet credit risk
		(NIS millions)			
First charge: financing ratio	Up to 60%	**37,175**	**3,038**	**28,542**	**762**
	Above 60%	**30,578**	**1,587**	**24,177**	**372**
Second charge or without charge		**740**	**43**	**600**	**1,061**
Total		**68,493**	**4,668**	**53,319**	**2,195**

		31 December 2012			
		Total[2]	Of which: bullet[2] and balloon	Of which: variable interest[2]	Total off-balance sheet credit risk
		(NIS millions)			
First charge: financing ratio	Up to 60%	32,413	2,901	25,351	2,265
	Above 60%	30,108	1,900	23,649	1,646
Second charge or without charge		834	61	659	23
Total		63,355	4,862	49,659	3,934

(1) Credit to the public, credit to governments, deposits in banks (in 2013, excluding deposits in the Bank of Israel) and other debts, excluding bonds and securities borrowed or purchased under agreements to resell.

(2) The ratio between the approved facility when the facility was granted and the value of the property, as approved by the Bank when the facility was granted. The LTV ratio is another indication of the Bank as to the assessment of customer risk when the facility was granted. On a quarterly basis, the minimum collective allowance of 0.35% is examined as required in Bank of Israel directives against the ratio of 0.75% required on credit with an LTV higher than 60%. It should be noted that the collective allowance is higher than the allowance required according to the LTV.

Note 4 – Credit Risk, Credit to the Public and the Allowance for Credit Losses (cont'd)

C. Credit to the public and off-balance sheet credit risk by size of credit of borrower

Credit limit		31 December 2013		
		Number of borrowers (3)	Credit (1)	Off-balance sheet credit risk (2)
(NIS thousands)			(NIS millions)	
From	To			
0	10	818,393	719	1,493
10	20	349,560	1,947	3,397
20	40	436,336	5,048	7,809
40	80	355,994	10,838	9,365
80	150	209,872	16,358	6,175
150	300	134,733	24,178	3,460
300	600	76,532	28,660	2,497
600	1,200	29,080	20,275	3,006
1,200	2,000	6,824	8,168	1,992
2,000	4,000	4,198	8,902	2,335
4,000	8,000	2,272	9,737	2,691
8,000	20,000	1,799	17,391	5,461
20,000	40,000	817	15,722	6,454
40,000	200,000	688	35,878	18,538
200,000	400,000	107	14,980	13,871
400,000	800,000	42	10,814	11,916
800,000	1,200,000	9	6,564	2,188
1,200,000	1,600,000	5	4,382	2,539
1,600,000	2,000,000	2	519	2,795
2,000,000	2,400,000	3	2,607	3,777
2,400,000	2,800,000	1	2,376	41
2,800,000	3,200,000	-	-	-
3,200,000	3,523,640	1	2,941	583
Total		2,427,268	249,004	112,383

Commencing with a credit level of NIS 8,000 thousand, the classification is set out by the specific consolidation method; with respect to the other borrowers, credit has been classified by the category consolidation method.

(1) Before the effect of allowances for credit losses, and before the effect of collateral permitted for deduction for purposes of single borrower and group of borrowers indebtedness; with the addition of the fair value of derivative instruments in the amount of NIS 4,247 million. Open credit card transactions have been allocated to credit levels by the category consolidation method.

(2) Credit risk in off-balance sheet financial instruments as calculated for purposes of single borrower restrictions.

(3) Number of borrowers by total credit and credit risk.
The definition of "borrower" and the definition of debt, including off-balance sheet credit risk, are in accordance with the directives of the Banking Supervision Department for amendment of Proper Conduct of Banking Business Directive No. 313 - "Restrictions on the Debt of a Single Borrower and of a Group of Borrowers".

Note 4 – Credit Risk, Credit to the Public and the Allowance for Credit Losses (cont'd)

C. Credit to the public and off-balance sheet credit risk by size of credit of borrower (cont'd)

Credit limit		31 December 2012 (4)		
		Number of borrowers (3)	Credit (1)	Off-balance sheet credit risk (2)
(NIS thousands)			(NIS millions)	
From	To			
0	10	773,134	764	1,494
10	20	325,954	1,769	3,236
20	40	392,182	4,423	7,188
40	80	309,081	8,723	8,920
80	150	155,540	10,493	6,064
150	300	83,794	13,631	3,219
300	600	58,307	21,770	2,387
600	1,200	36,118	26,464	3,053
1,200	2,000	9,748	12,593	2,089
2,000	4,000	5,191	11,481	2,572
4,000	8,000	2,509	10,712	3,065
8,000	20,000	1,825	17,799	5,303
20,000	40,000	885	17,619	6,878
40,000	200,000	741	39,400	19,373
200,000	400,000	112	16,652	13,675
400,000	800,000	46	15,028	10,720
800,000	1,200,000	9	4,464	4,222
1,200,000	1,600,000	5	5,723	1,052
1,600,000	2,000,000	-	-	-
2,000,000	2,400,000	3	4,312	2,122
2,400,000	2,800,000	-	-	-
2,800,000	3,200,000	1	2,878	62
3,200,000	3,301,000	1	2,175	1,126
Total		2,155,186	248,873	107,820

Commencing with a credit level of NIS 8,000 thousand, the classification is set out by the specific consolidation method; with respect to the other borrowers, credit has been classified by the category consolidation method.

(1) Net of specific provisions for doubtful debts and with the addition of the fair value of derivative instruments in the amount of NIS 3,495 million. Open credit card transactions were allocated to credit levels by the category consolidation method.

(2) Credit risk in respect of off-balance sheet financial instruments as calculated for purposes of single borrower restrictions.

(3) Number of borrowers by total credit and credit risk.

(4) Reclassified.

D. Information on loans sold

Proceeds of NIS 718 million were received for commercial loans sold in 2013 (NIS 234 million in 2012).

Note 5 – Credit to Governments

	31 December 2013	31 December 2012
	(NIS millions)	
Credit to the government	**338**	283
Credit to foreign governments	**220**	159
Total credit to governments	**558**	442

Note 6 - Investments in and Details of Investee Companies

A. Composition

	31 December 2013	31 December 2012
	Companies included on equity basis	Companies included on equity basis
	(NIS millions)	
Total investments in shares on equity basis (including other assets and goodwill)	**1,689**	2,129
Total		
Of which: post-acquisition profits	**1,005**	1,360
Post-acquisition items accrued in equity:		
Adjustments in respect of companies included on equity basis	**(141)**	(52)
Details regarding goodwill and other intangible assets:		
Amortization period	**0-20 years**	0-20 years
Original amount, net	**228**	218
Unamortized balance	**157**	151

Details of book value and market value of quoted investments:

	31 December 2013		31 December 2012	
	Book value	Market value	Book value	Market value
	(NIS millions)			
The Israel Corporation Ltd.	**1,137**	**2,526**	1,568	3,367

B. Group's equity in profit of companies included on equity basis:

	2013	2012	2011
	(NIS millions)		
Group's equity in profits of companies included on equity basis	**(313)**	(31)	143
Provision for deferred taxes	**20**	(36)	5
Group's equity in after-tax profits of companies included on equity basis	**(293)**	(67)	148

Note 6 - Investments in and Details of Investee Companies (cont'd)

C. Details regarding investee companies

(1) Holdings in Non-banking Holding Corporations (Conglomerates)

The Bank's holdings in non-banking corporations are subject to restrictions prescribed in the Banking (Licensing) Law, 1981 (the "Banking Law"). The Banking Law prescribes, *inter alia*, in Section 24A of the Law, that a banking corporation may hold more than 1% of the means of control in only one conglomerate (a corporation whose capital is more than some NIS 2,000 million and that operates in more than three branches of the economy). The Bank holds one conglomerate - The Israel Corporation.

It should be noted that under the legislation passed pursuant to the capital market reform, a Bank is allowed to hold five percent of the capital of an insurance company and ten percent of the capital of a corporation controlling an insurance company. In addition, under the amendment to the Banking (Licensing) Law in March 2010, a Bank is allowed to hold only one insurance company whose shareholders' equity under Section 35 of the Financial Services Supervision Law (Insurance), 1981, exceeds NIS 2,000 million.

(2) Details of a subsidiary company consolidated for the first time

On 10 February 2011, an agreement (hereinafter: "the purchase agreement") was signed between Bank Leumi Le-Israel Ltd. (hereinafter: "Leumi"), directly or through a company under its control, and Island Tower Foundation, Helena S. Safdié, Levy Edmundo Safdié, and G.RS. Participations S.A.R.L., the owners of the Bank Safdié SA in Switzerland (hereinafter: “Bank Safdié”), according to which Leumi will purchase, directly or through a company under its control, all of the share capital in the acquired bank, subject to conditions precedent specified in the agreement. On 30 November 2011, after the fulfilling of the conditions precedent appearing in the agreement, the purchase transaction was completed and Leumi acquired all of the share capital of Bank Safdié. In accordance with the purchase agreement, the total consideration paid on the date of closing was about SFR 143 million, of which SFR 110 million was paid to the sellers and the balance of SFR 33 million was deposited in trust to secure adjustments to the proceeds deriving from changes in the assets under management by Bank Safdié during the 24-month period following the date of the transaction’s closing, and additional adjustments according to formulas agreed upon by the parties. The surplus cost amounted to NIS 138 million. NIS 53 million less a reserve for future tax was attributed to customer portfolios. On 3 January 2012, the merger was formally completed in the context of which the activities of Bank Safdié merged with the activities of Bank Leumi Switzerland.

	At acquisition date (NIS millions)
Total assets (1)	3,141
Balance of attributed surplus cost less reserve for future tax	53
Balance of goodwill created on acquisition of subsidiary	85
Net profit attributed to Bank's shareholders at date of acquisition	2

(a) As reported by the Bank.

(3) Details of impairment

In light of the change in regulations in the international private banking field worldwide, and in Switzerland in particular, which increase the cost of service, and in light of the effect anticipated from these changes also on Leumi Private Bank (formerly Bank Leumi Switzerland), the Bank depreciated the balance of goodwill by NIS 76 million.

Note 6 - Investments in and Details of Investee Companies (cont'd)

D. Details concerning principal investee companies

1. Consolidated subsidiaries[1]

Name of company	Details of the company	Percentage of equity granting a right to profits 31 December 2013	2012	Percentage of voting rights 31 December 2013	2012	Investment in shares - net asset value 31 December 2013	2012
		(%)	(%)	**(%)**	(%)	(NIS millions)	
In Israel							
Arab-Israel Bank Ltd.	General banking services	99.7	99.7	**99.7**	99.7	**550**	524
Leumi Agricultural Development Ltd.		100.0	100.0	**100.0**	100.0	**58**	58
Leumi Industrial Development Ltd.		99.6	99.6	**99.8**	99.8	**105**	105
Leumi Partners Ltd. (3)	Business and financial services	100.0	100.0	**100.0**	100.0	**676**	426
Leumi Tech Ltd. (4)	Equipment leasing and granting loans	99.5	99.5	**99.8**	99.8	**986**	964
Leumi Finance Company Ltd.	Raising capital by bond issues	100.0	100.0	**100.0**	100.0	**157**	158
Leumi Card Ltd.	Provision of credit card services	80.0	80.0	**80.0**	80.0	**1,122**	986
Leumi Securities and Investments Ltd.		100.0	100.0	**100.0**	100.0	**21**	19
Leumi Capital Market Services Ltd.	Operating services to provident and mutual funds	100.0	100.0	**100.0**	100.0	**38**	34
Leumi Financial Holdings Ltd.	Financial holdings	100.0	100.0	**100.0**	100.0	**503**	474
Abroad							
Bank Leumi le-Israel Corporation	Holding company - registered in the U.S.	100.0	100.0	**100.0**	100.0	**504**	540
Bank Leumi USA (5)	General banking services - registered in the U.S.	99.9	99.9	**99.9**	99.9	**1,897**	2,016
Bank Leumi (UK) plc	General banking services - registered in the U.K.	99.8	99.8	**99.8**	99.8	**725**	792
Leumi Private Bank	General banking services - registered in Switzerland	94.8	94.8	**98.6**	98.6	**956**	1,060
Leumi Re Ltd.	Insurance	100.0	100.0	**100.0**	100.0	**81**	93
Bank Leumi (Luxembourg) SA	General banking services - registered in Luxembourg	100.0	100.0	**100.0**	100.0	**164**	153
Bank Leumi Romania S.A.	General banking services - registered in Romania	99.9	99.9	**99.9**	99.9	**247**	254
Companies held by Bank Leumi USA							
Leumi Financial Corporation (6)		99.9	99.9	**99.9**	99.9	**4,827**	5,176
Leumi USA Investment Corporation (6)		99.9	99.9	**99.9**	99.9	**3,426**	3,720

See notes below.

Balance of goodwill and intangible assets		Other equity investments (7)		Contribution to net profit attributed to shareholders of the banking corporation		Loss on impairment		Dividend recorded		Other items in accumulated shareholders' equity (2)		Guarantees for the company in favour of parties outside the Group	
31 December		31 December		31 December		31 December		31 December		31 December		31 December	
2013	2012	**2013**	2012	**2013**	2012	**2013**	2012	**2013**	2012	**2013**	2012	**2013**	2012
-	-	**104**	157	**106**	103	**-**	-	**80**	-	**-**	-	**-**	-
-	-	**-**	-	**-**	1	**-**	-	**1**	2	**-**	-	**-**	-
-	-	**-**	-	**1**	2	**-**	-	**1**	2	**-**	-	**-**	-
-	-	**1,195**	1,177	**213**	(68)	**-**	-	**-**	-	**37**	115	**578**	552
-	-	**-**	-	**22**	27	**-**	-	**-**	-	**1**	-	**2**	2
-	-	**-**	-	**13**	12	**-**	-	**13**	12	**-**	4	**-**	-
-	-	**-**	-	**160**	144	**-**	-	**-**	-	**-**	-	**-**	-
-	-	**-**	-	**2**	2	**-**	-	**-**	1	**-**	-	**-**	-
-	-	**-**	-	**4**	4	**-**	-	**-**	-	**-**	-	**-**	-
-	-	**-**	-	**5**	8	**-**	-	**-**	-	**-**	-	**-**	-
-	-	**-**	-	**1**	-	**-**	-	**-**	-	**(38)**	(13)	**-**	-
-	-	**-**	-	**64**	90	**-**	-	**-**	-	**(183)**	(51)	**52**	56
-	-	**480**	505	**(66)**	42	**-**	-	**-**	-	**-**	5	**-**	-
61	146	**186**	195	**(57)**	(18)	**-**	-	**-**	-	**(41)**	20	**-**	-
-	-	**-**	-	**5**	9	**-**	-	**18**	-	**-**	-	**-**	-
-	-	**40**	56	**10**	15	**-**	-	**-**	-	**2**	8	**25**	12
-	-	**-**	-	**(7)**	8	**-**	-	**-**	-	**-**	17	**10**	49
-	-	**-**	-	**(349)**	(87)	**-**	-	**-**	-	**-**	-	**-**	-
-	-	**-**	-	**(233)**	(22)	**-**	-	**61**	-	**-**	-	**-**	-

Note 6 - Investments in and Details of Investee Companies (cont'd)

D. Details concerning principal investee companies (cont'd)

2. Companies included on equity basis

		31 December		31 December	
		2013	2012	**2013**	2012
Name of company	Details of the company	Percentage of equity granting a right to profits		Percentage of voting rights	
		(%)	(%)	**(%)**	(%)
The Israel Corporation Ltd.	Holding company	**18.1**	18.1	**18.1**	18.1

(1) Data regarding consolidated companies reflecting the Bank's investment therein less investments of each company in other companies in the Bank Group, and the Bank's share in their results less each company's share in the results of other companies in the Bank Group in respect of the abovementioned investments.
(2) Including adjustments in respect of presentation of the securities available for sale of consolidated companies by fair value.
(3) The Bank's share in a capital reserve in respect of the benefit in controlling shareholders' loans is NIS 100 million.
(4) The Bank's share in a capital reserve in respect of the benefit in controlling shareholders' loans is NIS 82 million.
(5) The investment in the company was made by Bank Leumi Le-Israel Corporation.
(6) Property companies established by Bank Leumi U.S.A. and consolidated in their financial statements. The companies have shareholders' equity against credit transferred from Bank Leumi U.S.A. As a result of adjustment of the financial statements and translation thereof into shekels, income (losses) was generated on the consolidated capital, which are offset from Bank Leumi U.S.A.
(7) Other equity investments include capital notes and shareholders' loans.
(8) The balance of goodwill less accumulated losses for impairment of goodwill has been included in the column for investment in shares at net asset value.
(9) The data regarding companies included on equity basis is on a consolidated basis.
(10) Includes translation adjustment reserves and other funds accumulated in retained earnings.

Note 6 - Investments in and Details of Investee Companies (cont'd)

Balance of goodwill and intangible assets		Investments in shares at book value		Investments in shares at market value		Contribution to net profit attributed to shareholders of the banking corporation		Dividend recorded		Other items in accumulated shareholders' equity (12)		Guarantees for the company in favour of parties outside the Group	
31 December		31 December		31 December		31 December		31 December		31 December		31 December	
2013	2012	**2013**	2012	**2013**	2012	**2013**	2012	**2013**	2012	**2013**	2012	**2013**	2012
31	36	**1,137**	1,568	**2,526**	3,367	**(340)**	(110)	**-**	81	**(42)**	(22)	**30**	109

Merger of Leumi Mortgage

On 9 September 2012, the Board of Directors of the Bank approved the merger of Leumi Mortgage Bank with the Bank. On 10 September 2012, the Board of Directors of Leumi Mortgage Bank approved the implementation of the said merger. The merger took place on 31 December 2012 ("the Merger Date").

As at 31 December 2012, the merger was completed and was registered with the Registrar of Companies, after all of the preconditions for its conclusion had been fulfilled.

The merger which was executed is a statutory merger, whereby Leumi Mortgage transferred its assets and liabilities to the Bank, and Leumi Mortgage was dissolved without liquidation, pursuant to the provisions of Chapter 1 of the Eighth Part of the Companies Law, 1999, and subject to the provisions of Chapter 2 in the second part of the Income Tax Ordinance, such that on completion of the merger, Leumi Mortgage ceased to exist.

With effect from 15 January 2013, the banking license of Leumi Mortgage Bank was canceled.

Note 6 - Investments in and Details of Investee Companies (cont'd)

E. Goodwill and Intangible Assets

	Goodwill	Customer securities portfolios	Total
	(NIS millions)		
Cost			
As at 31 December 2011	**188**	**138**	**326**
Additions	1	-	1
Update pursuant to allocation of surplus cost (1)	85	(55)	30
As at 31 December 2012	**274**	**83**	**357**
Additions	**-**	**-**	**-**
As at 31 December 2013	**274**	**83**	**357**
Amortization and losses from impairment			
As at 31 December 2011	**144**	**1**	**145**
Amortization for the year	12	11	23
As at 31 December 2012	156	12	168
Amortization for the year	-	14	14
Loss from impairment	76	-	76
As at 31 December 2013	**232**	**26**	**258**
Amortized balance at 31 December 2013	**42**	**57**	**99**
Book value			
As at 31 December 2011	44	137	181
As at 31 December 2012	118	71	189
As at 31 December 2013	**42**	**57**	**99**

(1) Update pursuant to updated estimate for allocation of surplus cost in a business combination.

Note 7 – Buildings and Equipment

A. Composition

	Buildings and real estate (1)	Equipment, furniture and vehicles	Software	Total
	(NIS millions)			
Cost				
As at 31 December 2011	3,338	3,025	4,136	10,499
Additions	70	269	496	835
Disposals	(11)	(50)	(32)	(93)
Translation adjustment reserve	(2)	(1)	-	(3)
As at 31 December 2012	3,395	3,243	4,600	11,238
Additions	**70**	**171**	**481**	**722**
Disposals	**(41)**	**(15)**	**(103)**	**(159)**
Translation adjustment reserve	**(2)**	**(5)**	**-**	**(7)**
As at 31 December 2013	**3,422**	**3,394**	**4,978**	**11,794**
Accumulated depreciation				
As at 31 December 2011	1,716	2,397	2,733	6,846
Provision in the reporting year	83	181	464	728
Recognized losses from impairment	47	-	-	47
Disposals	(9)	(47)	(31)	(87)
Translation adjustment reserve	(1)	-	-	(1)
As at 31 December 2012	1,836	2,531	3,166	7,533
Provision in the reporting year	**82**	**175**	**516**	**773**
Recognized losses from impairment	**(5)**	**-**	**-**	**(5)**
Disposals	**(32)**	**(12)**	**(101)**	**(145)**
As at 31 December 2013	**1,881**	**2,694**	**3,581**	**8,156**
Amortized balance as at 31 December 2013	**1,541**	**700**	**1,397**	**3,638**
Balance after depreciation as at 31 December 2012	1,559	712	1,434	3,705
Balance after depreciation as at 31 December 2011	1,622	628	1,403	3,653

(1) Including leasehold installations and improvements.

B. Average rate of depreciation:

	31 December 2013	31 December 2012
Buildings and real estate	**3.38%**	3.31%
Equipment, furniture and motor vehicles	**18.92%**	16.16%
Software	**19.50%**	16.88%

Note 7 – Buildings and Equipment (cont'd)

C. The Group has rental or lease rights on real estate and equipment for a period of 1 to 94 years from the balance sheet date in an amount (net of depreciation) of NIS 134 million (31 December 2012 – NIS 134 million).

D. Investment property - buildings and real estate not used by the Group, mainly rental buildings, amount to NIS 26 million in the balance sheet (31 December 2012 – NIS 28 million).

E. The item "Buildings and equipment" includes improvements and leasehold rights, including payments on account. Some of the buildings are on leased land. Assets in the amount of NIS 216 million (31 December 2012 – NIS 209 million) in the balance sheet have not yet been registered in the name of the Bank at the Land Registry Office. The principal reasons for the non-registration are the absence of a land registry arrangement in the area ("parcellation"), and non-registration of the project as a condominium building by the contractor/developer.

F. Buildings earmarked for sale, in the amount of NIS 66 million (31 December 2012 – NIS 62 million) are shown net of a provision for anticipated losses. The fair value of the assets earmarked for sale at 31 December 2013 was NIS 141 million (31 December 2012 - NIS 101 million).

G. The balance of software includes costs capitalized during the year relating to the development of computer software in the amount of NIS 95 million (31 December 2012 – NIS 228 million).

Note 8 – Other Assets

	31 December 2013	31 December 2012
	(NIS millions)	
Deferred tax asset, net - see Note 26.I.	**2,955**	2,598
Excess of funds allocated for severance pay over provision – see Note 15.C	**771**	333
Assets transferred to ownership of the Group as a result of settlement of problem loans	**11**	12
Value of insurance policies in foreign branch	**378**	404
Excess of advance tax payments over current provisions	**66**	60
Expenses to be amortized on issuance of debentures, bonds and subordinated notes	**43**	57
Accrued income	**161**	167
Prepaid expenses	**189**	226
Other receivables and prepayments	**428**	672
Total other assets	**5,002**	4,529

Note 9 – Deposits of the Public

A. Types of deposits by location raised and type of depositor

	31 December 2013	31 December 2012(1)
	(NIS millions)	
In Israel		
On demand		
Non-interest bearing	**800**	714
Interest bearing	**78,022**	57,548
Total on demand	**78,822**	58,262
Fixed term	**177,970**	198,186
Total deposits in Israel[2]	**256,792**	256,448
Outside Israel		
On demand		
Non-interest bearing	**14,634**	16,358
Interest bearing	**840**	735
Total on demand	**15,474**	17,093
Fixed term	**13,737**	15,997
Total deposits outside Israel	**29,211**	33,090
Total deposits of the public	**286,003**	289,538
[2]Of which:		
Deposits of private persons	**125,774**	136,847
Deposits of institutional entities	**29,554**	22,059
Deposits of corporations and others	**101,464**	97,542

See notes on next page.

B. Deposits of the public by size on consolidated basis

	31 December 2013	31 December 2012(1)
	(NIS millions)	
Up to 1	**88,210**	91,006
From 1 to 10	**79,246**	86,528
From 10 to 100	**53,138**	53,321
From 100 to 500	**33,405**	34,260
Above 500	**32,004**	24,423
Total	**286,003**	289,538

(1) As of 31 December 2013, the Bank implements the circular of the Banking Supervision Department regarding disclosure of deposits, except for the disclosure requirements of deposits of institutional entities raised in Israel which the Bank has implemented as of 1 January 2013. The directive includes, inter alia, a distinction between disclosure of deposits raised in Israel and those raised abroad and a new disclosure requirement by size. The Bank applied the directive retroactively. See Note 1.

Note 10 - Deposits from Banks

	31 December 2013	31 December 2012(1)
	(NIS millions)	
In Israel		
Commercial banks:		
Demand deposits	**2,563**	2,295
Time deposits	**1,040**	1,007
Acceptances	**506**	428
Central banks:		
Demand deposits	**60**	28
Time deposits	**-**	-
Outside Israel		
Commercial banks:		
Demand deposits	**-**	-
Time deposits	**3**	2
Acceptances	**64**	52
Central banks:		
Demand deposits	**67**	75
Time deposits	**7**	186
Total deposits from banks	**4,310**	4,073

(1) As of 31 December 2013, the Bank implements the circular of the Banking Supervision Department regarding disclosure of deposits, except for the disclosure requirements of deposits of institutional entities raised in Israel which the Bank has implemented as of 1 January 2013. The directive includes, inter alia, a distinction between disclosure of deposits raised in Israel and those raised abroad and a new disclosure requirement by size. The Bank applied the directive retroactively. See Note 1.

Note 11 – Debentures, Bonds and Subordinated Notes

	Average duration (1) (years)	Internal rate of return (1) %	31 December 2013	2012
			(NIS millions)	
Debentures and notes (2):				
In Israeli currency linked to the CPI	**1.6**	**5.0**	**980**	1,282
Subordinated notes (2):				
Unlinked Israeli currency	**4.5** (3)	**2.8**	**4,554**	6,301
In Israeli currency linked to the CPI (4)	**3.5** (3)	**2.0**	**19,897**	19,932
In Swiss Francs	**5.3** (3)	**4.1**	**10**	10
Total debentures, notes and subordinated notes (5) (6)			**25,441**	27,525

(1) The average duration is the average of the payment periods, weighted according to the payment flow discounted at the internal rate of return. The internal rate of return is the rate of interest discounting the value of the anticipated future flow of payments to the amount included in the balance sheet.

(2) The unamortized balance of the discount less the premium on debentures and on subordinated notes not yet charged to profit and loss has been deducted from the amount of the debentures.

(3) The average duration as of the date of change in interest is based on a calculation of the effective average duration as calculated for purposes of Exhibit D. In unlinked subordinated notes it is 2.01 years, in those linked to the CPI it is 3.64 years and in subordinated notes in Swiss Francs is 0.80 years.

(4) Of which: subordinated notes (unquoted) deemed Upper Tier 2 capital in the amount of NIS 520 million (31 December 2012 - NIS 510 million) that in certain circumstances may be converted into shares.

(5) On 16 May 2011, in accordance with a permit received from the Israel Securities Authority, the Leumi Finance published a shelf prospectus for the issue of up to 9 series of debentures (series 179 to 187), up to 11 series of subordinated notes (Series N to W) for NIS 4 billion nominal value of each. In addition, the shelf prospectus allows for the issue of up to NIS 2,950,000,000 nominal value of subordinated notes (Series L) and NIS 3,350,000,000 nominal value of subordinated notes (Series M), in the framework of an expansion of quoted series first issued by means of a shelf prospectus dated 14 September 2010. The shelf prospectus dated 16 May 2011 is valid for two years from its publication.

According to the Shelf Offer Report dated 7 September 2011, Leumi Finance issued a total of about NIS 1.4 billion subordinated notes in the expansion to Series L – M as set out below:

Subordinated notes in the expansion of Series L amounting to NIS 1,142,941,000 par value (proceeds of NIS 1,144,083,941) are due to be repaid in one installment on 10 September 2017, are linked (principal and interest) to the consumer price index for July 2010 and bear interest at 2.6% per annum, payable on 10 September of each year from 2012 to 2017 (inclusive).

Subordinated notes in the expansion of Series M amounting to NIS 276,039,000 par value (proceeds of NIS 275,486,922) are due to be repaid in one installment on 10 September 2017, are not linked (principal and interest) to the any index and bear interest at 5.4% per annum, payable on 10 September of each year from 2012 to 2017 (inclusive).

The subordinated notes have been approved by the Bank of Israel as lower Tier 2 capital.

According to the Shelf Offer Report of 9 November 2011, Leumi Finance issued a total of some NIS 2 billion of subordinated notes in the expansion of Series L and an issue of Series N as follows:

Subordinated notes in the expansion of Series L amounting to NIS 1,078,669,000 par value (proceeds of NIS 1,105,635,725). For further details in respect of Subordinated Notes Series L, see above.

Subordinated notes in the expansion of Series N amounting to NIS 860,745,000 par value are due to be repaid in one installment on 9 November 2020, are linked (principal and interest) to the consumer price index for September 2011 and bear interest at 3.4% per annum, payable on 10 November of each year from 2012 to 2020 (inclusive).

The subordinated notes have been approved by the Bank of Israel as lower Tier 2 capital.

(6) In 2012, the company made one issue to the public pursuant to a shelf prospectus published on 15 May 2011 and a Shelf Offer Report published on 25 January 2012. In this issue, subordinated notes (Series M) and subordinated notes (Series N) in expansion of the quoted series, as follows:

1. NIS 1,280,000,000 par value subordinated notes (Series M), due to be repaid in one installment on 10 September 2017, not linked (principal and interest) to any index and bearing interest at 5.4% per annum (effective interest 5.1%), payable on 10 September of each year from 2012 to 2017. Pursuant to the results of the offer, conducted on the unit price, subordinated notes (Series M) were issued at a price of NIS 1.035 for each NIS 1 par value, for proceeds of NIS 1,324,800,000).

2. NIS 1,010,000,000 par value subordinated notes (Series N), due to be repaid in one installment on 10 November 2020, linked (principal and interest) to the CPI index and bearing interest at 3.4% per annum (effective interest 3.35%), payable on 10 November of each year from 2012 to 2020. Pursuant to the results of the offer, conducted on the unit price, subordinated notes (Series N) were issued at a price of NIS 1.011 for each NIS 1 par value, for proceeds of NIS 1,021,110,000).

Subordinated notes (Series M-N) that were issued as stated, were listed for trading on the Tel Aviv Stock Exchange. And the proceeds that the company received from their issue were deposited in Bank Leumi for use at its discretion and on its responsibility, on the same repayment and linkage terms as the terms of the same series and at the same interest rate as the series with the additional margin of 0.1% per annum.

Note 12 - Other Liabilities

	31 December 2013	31 December 2012
	(NIS millions)	
Deferred tax liability, net – see Note 26.I.	**140**	144
Excess of current provisions for taxes over advance payments	**310**	68
Excess of provisions for severance pay and pensions over amounts allocated - see Note 15.C.	**5,524**	4,960
Provisions for unutilized vacations and long service bonuses	**931**	912
Deferred income	**597**	460
Allowance for credit losses in respect of off-balance sheet items	**412**	447
Accrued expenses in respect of salaries and related expenses	**632**	306
Payables in respect of credit cards	**6,156**	5,931
Accrued expenses	**327**	344
Market value of securities sold short	**858**	484
Other payables and credit balances	**1,446**	1,520
Total other liabilities	**17,333**	15,576

Note 13 - Capital

A. Share capital

	31 December 2013		31 December 2012	
	Authorized	**Issued and paid***	Authorized	Issued and paid*
	(NIS)		(NIS)	
Ordinary shares of NIS 1.0 each	**3,215,000,000**	**1,473,551,221**	3,215,000,000	1,473,551,221

*All shares issued are registered in the names of the shareholders. Shares that have been or will be issued have been or will be converted into ordinary stock which is transferable in units of NIS 1.0.

The ordinary stock is listed on the Tel-Aviv Stock Exchange.

NIS 400.000,000 par value deferred index-linked deposits/capital notes (unquoted), issued in June and July 2002, and repayable on 30 June 2101, and that were recognized by the Bank of Israel as Upper Tier 2 capital of the Bank, are convertible, in certain circumstances defined by the Supervisor of Banks, according to the conversion formula as set out in the conditions of the deposit/capital, to 153,102,276 ordinary shares of the Bank, as of the date of the report.

B. Undertaking for allocation of shares

The remuneration policy for office holders of the Bank for the years 2013 and 2014 to 2016 determines, inter alia, the conditions for eligibility of office holders in the Bank for a performance-contingent annual bonus, insofar as they are eligible for a performance-contingent annual bonus.
In accordance with the provisions of Proper Conduct of Banking Business Directive 301A, fifty percent (50%) of the above variable annual bonus is awarded to office holders through blocked performance-dependent share units (PSU), with each PSU unit representing a deferred and contingent right to receive one ordinary share of NIS 1 par value of the Bank. The PSU units will be allocated to eligible office holders shortly after the report of the financial results of the banking system for the bonus year.

PSU units as mentioned above have not yet been allocated by the Bank.

Pursuant to the provisions of the remuneration policy, the rate of the overall cumulative amount of the PSU units to be allocated to all the senior officers (the Chairman of the Board of Directors, the President and Chief Executive Officer, and members of Bank Management) in respect of all the years covered by the bonus plan (2013 to 2016) will not exceed 0.38% of the issues and paid-up share capital of the Bank (see Note 15.G).

Note 13 – Capital (cont'd)

C. Dividend

The Bank did not distribute dividends in respect of the years 2011-2013.

(1) Restrictions on the distribution of dividends

In addition to restrictions under the Companies Law, a circular was issued on 15 January 2013 amending Proper Conduct of Banking Business Directive No. 331 concerning dividend distribution by banking corporations. In light of requirements added in recent years to the Public Reporting Directives making it mandatory to record certain profits and losses of the Bank in other comprehensive income and not in profit and loss, the tests for distributing a dividend were updated. Pursuant to the update, "distributable profits" include elements of other comprehensive income, and the Bank shall not carry out a dividend distribution (unless it received prior approval from the Supervisor), inter alia:

- When the cumulative balance of retained earnings, net of negative differences included in cumulative other comprehensive income is not positive, or if the amount of the proposed distribution would cause such a balance of retained earnings;
- When one or more of the last three calendar years ended in a loss or in a comprehensive loss;
- When the cumulative result of the three quarters ended at the end of the interim period for which the last financial statement has been published indicates a loss or a comprehensive loss.

It was further established that the Bank shall not perform distributions from capital reserves or from positive differences included in the statement of cumulative other comprehensive income.
The amendment came into effect as of 1 January 2013.

Furthermore, in the letter of the Supervisor of Banks on the subject of capital policy for interim periods, it was determined that a banking corporation shall not distribute a dividend if it does not have a core capital ratio of at least 7.5%, or if such distribution would cause a failure to comply with the aforesaid ratio. In the letter of the Banking Supervision Department, concerning minimum core capital ratios under Basel 3, the banks were required, inter alia, to refrain from distributing a dividend if as a result it may not meet the capital targets required in it (for further details, see Note 13A.E below).

Notwithstanding the above, in certain cases the Bank can distribute dividends even if the aforesaid circumstances apply, if it obtains prior written approval of the Supervisor of Banks for such distribution, up to the amount thus approved.

Note 13 - Capital Adequacy in accordance with the directives of the Supervisor of Banks

Regulatory capital and capital adequacy are calculated pursuant to Proper Conduct of Banking Business Directives Nos. 201-211 on the subject of "Capital Measurement and Adequacy" (Basel II)

	31 December 2013	31 December 2012
	(NIS millions)	
A. Consolidated data		
Capital for purposes of calculating capital ratio		
Tier 1 capital, after deductions	**26,263**	24,312
Tier 2 capital, after deductions	**15,007**	17,978
Total capital	**41,270**	42,290
Weighted balance of risk assets		
Credit risk	**247,548**	253,895 (3)
Market risk	**10,510**	9,710
Operational risk (2)	**20,426**	20,841
Total weighted balances of risk assets	**278,484**	284,446
Ratio of capital to risk assets		
Ratio of Tier 1 capital to risk assets	**9.43%**	8.55%
Ratio of total capital to risk assets	**14.82%**	14.87%
Ratio of total minimum capital required by the Supervisor of Banks	**9.00%**	9.00%
B. Principal subsidiary companies		
Arab Israel Bank		
Ratio of Tier 1 capital to risk assets	**11.85%**	10.84%
Ratio of total capital to risk assets	**12.50%**	14.76%
Ratio of total minimum capital required by the Supervisor of Banks	**9.00%**	9.00%
Leumi Card Ltd.		
Ratio of Tier 1 capital to risk assets	**16.00%**	16.00%
Ratio of total capital to risk assets	**16.00%**	16.00%
Ratio of total minimum capital required by the Supervisor of Banks	**9.00%**	9.00%
Bank Leumi USA (1)		
Ratio of Tier 1 capital to risk assets	**11.70%**	11.56%
Ratio of total capital to risk assets	**14.54%**	14.47%
Ratio of total minimum capital required by the local authorities	**10.00%**	10.00%

(1) The United States office is not obliged to calculate the capital adequacy ratio in accordance with Basel II. Accordingly, the ratios presented are according to Basel I.
(2) First Pillar capital allocation in respect of operational risk is in accordance with the Standardized Approach.
(3) Restated.

Note 13 - Capital Adequacy in accordance with the directives of the Supervisor of Banks (cont'd)

Regulatory capital and capital adequacy are calculated pursuant to Proper Conduct of Banking Business Directives Nos. 201-211 on the subject of "Capital Measurement and Adequacy" (Basel II) (cont'd)

	31 December 2013	31 December 2012
	NIS millions	
C. Capital components for purposes of calculating the capital ratio (consolidated data)		
Tier 1 capital		
Shareholders' equity	**26,244**	24,426
Minority interest of external shareholders in equity of consolidated subsidiaries	**340**	307
Less goodwill	**168**	235
Less intangible assets	**88**	105
Less losses from adjustment to fair value of securities available for sale	**-**	-
Less other deductions from Tier 1 capital	**65**	81
Total Tier 1 capital	**26,263**	24,312
Tier 2 capital		
a. Upper Tier 2 capital		
45% of net profits, before related tax effect, in respect of adjustments to fair value of securities available for sale	**100**	333
General provision for doubtful debts	**428**	428
Compound capital instruments	**6,149**	6,071
b. Lower Tier 2 capital		
Subordinated notes	**8,395**	11,228
c. Deductions from Tier 2 capital		
Investments in companies other than non-banking which have a significant effect	**61**	56
Other deductions	**4**	26
Total Tier 2 capital	**15,007**	17,978

Note 13 - Equity and Capital Adequacy in accordance with the directives of the Supervisor of Banks (cont'd)

D. Restrictions on housing loans

The Bank implements the provisions of the letter the Supervisor of Banks on the updating of guidelines on residential property that include new requirements regarding capital adequacy as follows:

- The risk weighting in respect of housing loans – stricter capital requirements were determined for housing loans granted from 1 January 2013. The new capital requirements are contingent on the LTV ratio as follows:
  - LTV less than 45% - a risk weighting of 35%
  - LTV above 45% but less than 60% - a risk weighting of 50%
  - LTV above 60% - a risk weighting of 75% (if eligible for regulatory retail credit) or more

- The credit conversion coefficient in respect of Sales Law guarantees after the delivery of an apartment – reduction of the credit conversion coefficient attributed to guarantees to secure the investment of apartment purchasers from 20% to 10%, if the apartment was delivered to the borrower. This reduction applies also to the percentage weighting of guarantees. This amendment applies retroactively.

On 29 August 2013, the Supervisor of Banks published a letter on restrictions on housing loans in which it was determined, inter alia, that a banking corporation is required to allocate a risk weighting of 100% for housing loans that were approved in principle from 1 September 2013 where the rate of repayment out of income exceeds 40%. The Bank implements the guidelines set out in the letter.

E. The expected effect of adoption of Basel III directives on 1 January 2014

In May 2013, the Supervisor of Banks amended Proper Conduct of Banking Business Directives No. 201-211 on capital measurement and adequacy, to adapt them to the Basel III guidelines. The amendments to the above directives will come into effect from 1 January 2014, with implementation in stages in accordance with transitional provisions set out in Proper Conduct of Banking Business Directive No. 299 on "Capital Measurement and Adequacy – Regulatory Capital – Transitional Provisions".

In addition, on 29 August 2013, a Banking Supervision Department circular was published on "Basel Disclosure Requirements relating to the Composition of Capital". The above circular set out updated disclosure requirements that banks will have to include as part of adopting the Basel III directives. The disclosure requirements will come into effect as of 1 January 2014. However, in the financial statements for 2013 the Bank was required to include a disclosure of the expected effect of adoption of the Basel III directives.

The expected effect of adoption of the Basel III directives on 1 January 2014 is shown below, as of the position of the Bank on 31 December 2013. In calculating the expected effect of adoption of the Basel III directives on 1 January 2014, the transitional provisions detailed above were taken into consideration.

It should be emphasized that the data brought in the estimate of the expected effect of implementing Basel III directives were prepared to our best understanding of the directives of the Banking Supervision Department in connection with the manner of implementation of the directives regarding the calculation of deductions from capital, regulatory adjustments, and implementation of other rules including rules regarding transitional provisions. In light of the complexity of the directive and related staff positions published by the Banking Supervision Department on their application, changes may occur in interpretation of the directive or the policy to be followed in its application in 2014 and thereafter.

Note 13 - Equity and Capital Adequacy in accordance with the directives of the Supervisor of Banks (cont'd)

E. The expected effect of adoption of Basel III directives on 1 January 2014 (cont'd)

	According to the instructions of the Supervisor of Banks applicable on 31 December 2013 (Basel II)	Expected effect of implementing Basel III	According to the instructions of Basel III	
	(NIS millions)			
A. Regulatory capital after deductions and regulatory adjustments				
Core capital				
Tier 1 capital (Basel III - Tier 1 shareholders' equity	26,263	157	26,420	
Tier 2 capital	15,007	(670)	14,337	
Total capital	41,270	(513)	40,757	
B. Weighted balances of risk assets				
Credit risk	247,548	8,564	256,112	
Market risk	10,510	-	10,510	
Operational risk	20,426	-	20,426	
Total weighted balances of risk assets	278,484	8,564	287,048	
C. Ratio of capital to risk components				
Tier 1 capital ratio (Basel III - Tier 1 shareholders' equity) to risk assets	9.43%	(0.23%)	9.20%	
Overall capital ratio to risk assets	14.82%	(0.62%)	14.20%	
Minimum capital ratio required under the directives of the Supervisor of Banks:				
Tier 1 shareholders' equity ratio	-	9.00%	9.00%	(1)
Overall capital ratio	9.00%	3.50%	12.50%	(1)

(1) Commencing as of 1 January 2015.

Note 13 - Equity and Capital Adequacy in accordance with the directives of the Supervisor of Banks (cont'd)

F. Capital Adequacy Target

Group policy, approved by the Board of Directors, which expresses its risk appetite, is to hold a level of capital adequacy higher than the threshold determined from time to time by the Bank of Israel, and higher than the rate required according to the results of the ICAAP. In addition, targets that the Group wishes to meet in the event of a stress scenario are defined.

On 30 May 2013, the Supervisor of Banks issued final directives for the adoption of Basel III recommendations in Israel, including an amendment of Proper Conduct of Banking Business Regulation 201 regarding "Measurement and Capital Adequacy, Introduction, Scope of Application and Calculation of Requirements". Pursuant to this directive, all banking corporations will be required to comply with a minimum Tier 1 capital ratio of 9% with effect from1 January 2015.

In addition, a large banking corporation, whose total balance sheet assets on a consolidated basis constitutes at least 20% of the balance sheet assets in the banking system in Israel, will be required to comply with a minimum Tier 1 capital ratio of 10%, with effect from 1 January 2017. This additional directive is applicable to Leumi.

Compliance with these targets will be achieved gradually. The Bank intends to maintain a planning margin above these targets.

In addition, all banking corporations in Israel will be required to maintain an overall capital ratio of 12.5% by 1 January 2015. A large banking corporation will be required to maintain an overall capital ratio of 13.5% by 1 January 2017 This additional provision applies to Leumi.

Following an analysis of the ICAAP risk map, the Board of Directors of the Bank decided to determine the Leumi Group's overall capital adequacy target to be not less than 13.5% over the long term.

The Bank is prepared to meet the requirements described above that comply with the requirements of the Supervisor of Banks as set forth in the directives.

Note 14 – Liens and Restrictive Conditions

As at 31 December 2013 and 31 December 2012, debentures and notes issued by consolidated companies in Israel are not secured by floating charges on their assets. Foreign branches and consolidated companies have pledged securities and other assets as security for deposits received from the Federal Home Loan Bank (FHLB) and certain obligations pursuant to requirements of the authorities of the countries in which they operate. Pledged assets amount to NIS 358 million (31 December 2012 - NIS 426 million). Total liabilities in respect of which assets were pledged amount to NIS 295 million (31 December 2012 - NIS 377 million).

The Bank executes short-term lending of securities in foreign currency from the available portfolio, via the Euroclear clearinghouse, for other customers of the clearinghouse, without knowing the identity of the borrowers. The lending is carried out under a full guarantee of the Euroclear clearinghouse which is an AA+ rated financial institution. The value of the balance of the securities lent to the Euroclear clearinghouse as of 31 December 2013 was about NIS 84 million (31 December 2012 - NIS 117 million).

As a member of the Tel Aviv Stock Exchange, the Bank is a member of the Risk Fund of the Stock Exchange Clearing System.

The amount of the Risk Fund is to be the average highest debit balance that the member had in the six months ending in the calendar month prior to the update. The Fund updates the amounts 4 times a year.

In addition – the bank has signed a credit facility of US$ 150 million with the Euroclear Clearing System to guarantee securities settlement by customers. The credit facility is backed up by securities held by the Bank in the Euroclear Clearing System.

Each of the members of the Risk Fund pledges securities in favor of the Stock Exchange Clearing System in the amount of its proportionate part in the fund, which secures the member's liabilities to the Clearing System and the member's share in the Risk Fund. Furthermore, such collateral also secures the liabilities of the other members of the Risk Fund, if the collateral that the other member provided is not sufficient to cover the other member's liabilities, and in accordance with the proportionate part of each of the members in the Fund, up to the amount of the collateral provided or up to the amount of the liabilities to the Stock Exchange Clearing System, whichever is the lower. The total of debentures and deposits pledged by the Bank to the Stock Exchange Clearing System as at 31 December 2012 was NIS 80 million (31 December 2012 – NIS 74 million).

The Bank is a member of the Maof Clearing System Risk Fund. The Bank has undertaken to the Maof Clearing System to pay every charge deriving from its Maof transactions for its customers, its nostro, and for Maof transactions of a member of the TASE not clearing independently through the Maof Clearing System. The total of the Bank's liabilities is shown in Note 18.A under Guarantees and Other Liabilities.

The Bank pledges collateral in favor of the Maof Clearing System in the amount of its proportionate part in the Risk Fund and also in respect of its above-mentioned liabilities, which secures its liabilities to the Maof Clearing System and its share in the Risk Fund. Furthermore, such collateral also secures the liabilities of the other members of the Risk Fund. In the event that the collateral that the other member provided were not sufficient to cover all of his liabilities, the Maof Clearing System is entitled to realize the collateral provided to it by the other members of the Risk Fund, in accordance with the proportionate part of each of the members in the fund, up to the amount of the collateral provided or up to the amount of the liabilities to the Maof Clearing System, whichever is the lower.

At the date of the financial statements, the Bank's share of the Maof Clearing System Risk Fund was NIS 145 million (about 12% of the Fund).

Note 14 – Liens and Restrictive Conditions (cont'd)

The Bank, like any other member of the Clearing System, is entitled to secure its liabilities to the Maof Clearing System risk fund by means of pledging government bonds and deposits. The total of the debentures pledged by the Bank to the Maof Clearing System in respect of the activity of the customers, the *nostro*, and risk fund as at 31 December 2013 was NIS 983 million (31 December 2012 – NIS 1,380 million).

The Bank participates in an arrangement for ensuring the finality of settlement in default situations in which there is an insufficient balance in the clearing account of one or more of the other participants, as a participant in the RTGS (*"Zahav"*) System, and a holder of a clearing account in the system and a member of the *Masav* payment system and the banking clearing system ("participant"). In the event of default, each non-defaulting participant ("surviving participant") is to bear the debit charges of the participant that defaulted, according to the relative share of the surviving participant divided by the difference between 100% and the relative share of the participant that defaulted. The relative share of the Bank at 31 December 2013 in the *Masav* system is 16.31% and in the bank clearing system – 22.57% (this percentage is updated every six months according to the relative weighting of debit charges of each participant that were passed through the payment system relevant to the previous six months). The total ceiling for participation for all participants is NIS 300 million in the clearing system and NIS 150 million in the bank clearing system. In the event of default, on the business day following the date of default, immediately after the system opens, the Bank of Israel will send a multi-party payment instruction debiting the clearing account of the defaulting participant and crediting the clearing accounts of the surviving participants with the amount that each surviving participant paid in the framework of the arrangement, with the addition of interest at the Bank of Israel rate. The default arrangement is not intended to deal with a situation of a known or probable insolvency. In the event of insolvency, the proceedings will be passed to the Banking Supervision Department.

The Bank and its consolidated companies engage with foreign banks in CSA (Credit Support Annex) agreements that are intended to reduce mutual credit risks created between the banks during trading in derivatives. Under the agreements a measurement is made on a periodic basis of the value of all derivatives transactions carried out between the parties and if the net exposure of one of the parties exceeds the predetermined limit that party is required to transfer to the other party deposits totaling the amount of exposure, until the next measurement date. At 31 December 2013, the Group had made deposits in favor of foreign banks totaling NIS 480 million (31 December 2012 – NIS 1,112 million).

The Bank and its consolidated companies engage with foreign banks into agreements under which amounts are deposited in the foreign banks for purposes of carrying out marketable futures transactions in exchanges abroad for them or their customers. As at 31 December 2013, the Group had deposited an amount of US$ 170 million in the above banks (31 December 2012 – US$ 268 million).

The Bank has signed a debenture, in accordance with which the Bank has pledged by way of a first fixed charge and assignment by way of pledge, unlimited in amount, in favor of the Bank of Israel, all of the assets and rights in specific accounts held in the name of the Bank of Israel, in the Tel Aviv Stock Exchange Clearinghouse, in Euroclear Bank or in any other clearinghouse to which the Bank and the Bank of Israel must agree. The mortgaged assets in the accounts of Euroclear Bank, or in another account maintained in the clearinghouse outside Israel, are also mortgaged under a first ranking floating lien in favor of the Bank of Israel.

This pledge is to secure all the liabilities of the Bank in connection with credit that the Bank of Israel has extended or will extend and the placing of collateral to secure it, as detailed in the credit documents, except for credit according to a credit agreement between the Bank of Israel and the Bank and a secured debenture dated May 21, 2008.

On 21 May 2008, the Bank signed a debenture, by which the Bank pledged by way of a first floating charge, in favor of the Bank of Israel, its rights to receive monetary amounts and charges in shekels, which are due or will be due to the Bank from time to time from its customers, that are corporations (which were incorporated under the laws of the State of Israel) not being in arrears in repayment to the Bank of credits received from the Bank,

Note 14 – Liens and Restrictive Conditions (cont'd)

in respect of credits in shekels of which the duration (average life) of each credit does not exceed three years, which were given or will be given by the bank to the above customers.

This pledge is to secure credits that the Bank of Israel will grant to the Bank for purposes of the Bank's activity as a supplier of liquidity services in shekels to the Continuous Linked Settlement Bank (CLS) Bank, with the addition of interest, costs and expenses involved in realizing the pledge, up to the amount of NIS 1.1 billion, in accordance with the terms of the credit agreement signed by the parties in this matter. Leumi did not avail itself of any such credit during 2010-2013.

	31 December 2013	31 December 2012
	(NIS millions)	
Sources of securities received which the Bank may sell or pledge, by fair value, excluding set-offs:		
Securities received in securities borrowing transactions against cash	**1,360**	1,435
Uses of securities received as collateral and securities of the Bank, by fair value, excluding set-offs:		
Securities loaned in securities lending transactions against cash	**624**	1,007

Apart from these securities, as at the date of the balance sheet, additional securities were given as collateral, shown under Securities above, which the lenders are not permitted to sell or pledge.

In September 2010, the Bank signed a deed of pledge, at the instructions of the Federal Reserve, under which it pledged monetary deposits in favor of Bank Leumi USA, in connection with loans given by Bank Leumi USA with collateral of obligations by Bank Leumi Le-Israel, in support of these obligations. The amount of the pledge at 31 December 2013 was US$ 44 million (31 December 2012 - US$ 49 million).

Note 15 – Employee Rights

A. Signing of collective labor agreement regarding privatization

On 17 November 2010, a special collective agreement was signed concerning the rights of employees, between the Bank and the representative body of employees of the Bank ("the Collective Agreement" or "the "Transaction") further to the agreement and resolution of the Board of Directors of the Bank. The Collective Agreement was approved by the Audit Committee, and thereafter, by the Board of Directors, on 21 November 2010, and by the General Meeting, on 28 December 2010. According to the Collective Agreement, the effectiveness of the consents to the abovementioned special collective agreement dated 30 November 2005 between the Bank and representatives of the employees ("the previous collective agreement") will be extended. Pursuant to the Collective Agreement, the consent that was in the previous collective agreement, to extend until 31 December 2010 the validity of the Employment Code and all collective agreements and arrangements, as well as all the agreements, procedures and practices granting rights to Bank employees, who are currently in the Bank, according to their individual status, was extended for a further period of four years – until 31 December 2014.

It was further provided in the collective agreement that the "industrial peace" undertaken by the representatives of the employees as stated in paragraph 7 of the previous collective agreement would continue to be in effect.

B. Severance pay and pensions

1. General

For employees that commenced their employment with the Bank since 1 January 1999 (hereinafter: "2nd generation employees") and had not yet received permanent employment status as at the signing date of the special collective bargaining agreement in 2000 covering a special pension arrangement, current deposits are made to a pension fund. The pension plan is a comprehensive cumulative pension plan with additional insurance for disability and death. The Bank will not have any pension liability in respect of these employees other than to supplement severance pay in accordance with the agreement.

Employees, who began working with the Bank before 1 January 1999 (hereinafter: ("1st generation employees") and have received permanent employment status before the date of signing the aforementioned agreement, that retire from the Bank at retirement age, except those mentioned above and in (3) below, may choose between the right to receive severance pay plus their accumulated provident fund, or the right to receive a pension in which case they relinquish their right to the severance pay and provident fund, subject to the provisions of the law. The entitlement to a pension is calculated at a pension rate of 40% for the first 15 years of employment, i.e. 2.67% per annum, and of 1.5% for each additional year, up to a maximum rate of 70%.

Provisions for severance pay are calculated on the basis of the latest salary, at one month's salary per each year of employment. Funds allocated for liabilities for severance pay are deposited in provident funds.

Provisions for pensions are based on an actuarial calculation that takes into account the change in the retirement age according to the Retirement Age Law, 2004. The actuarial calculation was made according to the accrued benefits valuation method, taking into account various parameters including the probability, based on past experience, of the rate of utilization of the pension benefits and the rate of withdrawal of severance and remuneration benefits (current utilization rate of pension rights is that about 76% choose a pension, while the remainder chose severance pay and provident funds), and past experience regarding disability, etc.

The actuarial calculation is based on the updated provisions of the Chief Actuary in the Ministry of Finance with respect to mortality rates from March 2013, which were determined by the Commissioner of the Capital Market, Insurance and Savings for insurance companies, as a result of the change in the rate of improvement in life expectancy, and that were adopted for the population of the Bank’s employees.

Calculation of the Bank's actuarial liability for pension payments is made using the capitalization rate determined by the Supervisor of Banks (4%) and on the assumption of a real increase in salary based on past experience and varying in accordance with the age of the employee.

The calculation is made under a comprehensive pension plan, which includes old age, disability and survivor pensions and also takes into account employees who have not yet completed the period required for receipt of pension benefits (15 years of service).

The balance sheet includes provisions based on the higher of the liabilities for severance pay plus provident benefits, and the pension liability. The Bank's pension liability for employees who have left and have opted for pension benefits, as well as that stated in (3) below, is covered by the pension provision, which is calculated based on the present value of the liability calculated by an actuary, as noted above.

2. Benefits to “Leumi Alumni”

“Leumi Alumni” are entitled to receive, in addition to their individual choice of a pension and/or severance payments, additional benefits which consist mainly of a holiday gift, a medical check-up (for some of the alumni) and participation in the cost of additional welfare and social activities.

“Leumi Alumni” – persons who, regardless of their age, have concluded working with the Bank after 25 years of employment, or have concluded working with the Bank at the legal retirement age after at least 15 years of employment.

The accumulated amount at 31 December 2013 for expected costs in respect of the above entitlements in the period following the employment period according to actuarial calculation amounts to some NIS 139 million (31 December 2012 - NIS 128 million).

3. Early retirement for employees under personal employment contracts

a. Ms. Rakefet Russak-Aminoach serves in the position of President and CEO of the Bank as of 1 May 2012. The monthly salary of the President and Chief Executive Officer is NIS 183,000 (linked to the increase in the last known index in January 2013). The President and CEO, who had a first generation employment agreement, transferred to the employment conditions of a second generation agreement as of 2013, as follows: the rights of the President and Chief Executive Officer to a non-contributory pension from the Bank pursuant to her rights as stated below will only be in respect of the frozen salary level (the salary of the President and Chief Executive Officer at the date of transfer from first generation to second generation plus linkage to the CPI), whereas her rights regarding salary increments above the frozen salary level will be pursuant to second generation conditions (provident fund and severance fund contributions without non-contributory pension rights from the Bank).

Pursuant to her terms of office and employment in the Bank, and in accordance with the update approved by the General Meeting of the Bank on 11 February 2014 (after

Note 15 – Employee Rights (cont'd)

approval of the Remuneration Committee and the Board of Directors) the President and Chief Executive Officer is entitled, in the event of termination of the employee-employer relationship between her and the Bank, to the following conditions: in the event of dismissal before completing three years in the position of President and Chief Executive Officer, the President and Chief Executive Officer will be entitled to severance pay of an amount equalling 250% of her last monthly salary multiplied by the number of years of her employment at the Bank, with the addition of provident fund contributions. In the event of dismissal after three years in the position of President and Chief Executive Officer or in the event of retirement, the President and CEO will be entitled to choose between (a) severance pay in the amount equivalent to 200% of her last monthly salary, multiplied by the number of years of her employment in the Bank, with the addition of provident fund contributions; and (b) an immediate retirement pension from the Bank pursuant to conditions of first generation that transferred to second generation. The rate of retirement pension to the President and CEO is as set out in sub-paragraph c. below concerning members of management. The definition of "dismissal" regarding the President and Chief Executive Officer includes resignation following deterioration in working conditions, including resignation as a consequence of changes that took place in the Bank and that do not allow the President and Chief Executive Officer to continue functioning as President and Chief Executive Officer, in the opinion of the President and Chief Executive Officer with approval of the Remuneration Committee or the Board of Directors. In the event of resignation before completing three years in her position as President and Chief Executive Officer, the President and Chief Executive Officer will be entitled to compensation of an amount equal to 100% of her last monthly salary multiplied by the number of years of her employment at the Bank, with the addition of provident fund contributions, whereas if the resignation is after completing three years of working in the Bank, the President and CEO will be entitled to compensation in the amount of 250% of her last monthly salary multiplied by the number of years of her employment at the Bank, with the addition of provident fund contributions.

The Bank and the President and CEO are each entitled to terminate the working relationship by giving advance notice of six months.

The Remuneration Committee, the Board of Directors, and the General Meeting confirmed (on 11 February 2014) that the President and Chief Executive Officer is entitled to an annual performance-contingent bonus and a fixed annual bonus, pursuant to and subject to the provisions of the remuneration policy for office holders in the Bank as set forth in paragraph G. below, for each of the years 2013, 2014, 2015, and 2016.

b. Members of the Management of the Bank who have a first generation employment agreement, transferred to the employment conditions of a second generation agreement as of 2013, as follows: their rights to a non-contributory pension from the Bank pursuant to the rights stated below will only be in respect of the frozen salary level (the salary at the date of transfer from first generation to second generation plus linkage to the CPI), whereas rights regarding salary increments above the frozen salary level will be pursuant to second generation conditions (provident fund and severance fund contributions without non-contributory pension rights from the Bank).

c. In accordance with first generation terms of employment, members of Management of the Bank (subject to that stated in sub-paragraph b. above) and a group of senior executives of the Bank (executive vice presidents, senior assistants to the CEO, and

Note 15 – Employee Rights (cont'd)

assistants to the CEO), are entitled, in the event of dismissal, to an immediate pension, if their age plus the number of years of employment with the Bank amounts to 75, or 80 under the new contracts. The years of service of a member of Management (if the employee served at least 7 years as a member of Management) will be counted as additional years of seniority for purposes of the said aggregate years of service.
The pension for members of Management will be calculated at the rate of 40% for the first 15 years of employment, i.e. 2.67% per annum, and 1.5% for each additional year until signing a personal contract, 2% for each year under a personal contract, and 2.5% for each year of service as a member of Management, up to a maximum rate of 70%. The pension for senior executives is calculated at the rate of 40% for the first 15 years of employment, i.e. 2.67% per annum, 1.5% for each additional year until signing a personal contract, and 2% for each year thereafter, up to a maximum rate of 70%. Alternatively, the said employees are entitled to choose, in the event of dismissal, severance pay at the rate of 200% (and 250% if their age plus the number of years of employment with the Bank does not amount to 75, or 80 as mentioned) of their latest monthly salary multiplied by the number of years of employment, plus the amounts accumulated to their credit in the provident fund. In such case, the employees are not entitled to a pension.

An employee who voluntarily resigns will be entitled to severance pay at the rate of 100%, plus the funds accumulated to his credit in the provident fund.

The Bank and the said employees are entitled to terminate the employee-employer relationship by giving advance notice of six months.

Personal employment contracts of members of Management of the Bank provide, inter alia, as follows: an employee who retires voluntarily at the age of 62 years or more will be entitled, upon fulfillment of a number of conditions, to severance pay at a rate of 200% plus accrued amounts in his provident. An employee who, upon termination of the employee-employer relationship did not utilize his special jubilee vacation will be entitled to an additional month of advance notice. In the cooling-off period, which does not coincide with the period of advance notice, the employee will be entitled to a salary and to related benefits.

According to the personal contracts with members of the management of the Bank, who are not 1st generation or 2nd generation in the Bank, in the event of dismissal, these members of Management will not be entitled to a pension from the Bank, but to compensation amounting to 250% of the last monthly salary for each year of employment in the Bank, with the addition of monies accrued in the provident fund from which are deducted the amounts accrued in the severance pay fund. Any employee, as aforesaid, who voluntarily resigns will be entitled to 100% of severance pay, plus the monies in the provident fund after deduction of the amounts accrued in the severance pay fund.

The Bank approved personal employment contracts for a group of senior managers from among the 2nd generation in the Bank, who are entitled to a pension plan as stated in the first paragraph of Note 15.B (1) above. These managers are not entitled to a first generation pension from the Bank. It was therefore stipulated in these personal contracts that the Bank undertook, in the event of dismissal, to pay compensation at the rate of 250% of the last monthly salary for each year of work in the Bank, together with provident fund allocations, after deduction of the amounts accrued in the severance pay fund.

If a manager is dismissed whose age is 55 or more, and whose period of service in the Bank is 25 years or more, the manager will be entitled to chose, on dismissal, between compensation at the rate of 200% of the last monthly salary for each year of work in the Bank, together with provident fund allocations, after deduction of the amounts accrued in the severance pay fund; or alternatively, receiving all the funds and rights in the compensation and provident fund, when until the date he will be entitled to receive them, under the terms of the rules of the fund and the provisions of the law, he will be entitled to receive a pension from the Bank.

The maximum additional expense that the Bank may incur in the event of the employees mentioned in the above paragraph being immediately dismissed amounts to NIS 388 million (including salary tax payable on the pension) (2012 – NIS 364 million). Since it is not likely that all the above mentioned employees will be dismissed immediately, the Bank recorded a provision at the rate of 25% of the above amount, in the amount of NIS 97 million (including salary tax) (2012 – NIS 110 million). The above amounts also include members of Management.

Part of the said provision was attributed specifically to members of Management, the balance of which at 31 December 2013 was NIS 24 million (31 December 2012 – NIS 12 million).

4. The Chairman of the Board of Directors of the Bank

The Audit Committee, the Board of Directors and the General Meeting of the Bank has approved the terms of employment of the Chairman of the Board of Directors, who is employed in a full-time position as Executive Chairman.

The Bank and the Chairman have the option of discontinuing the engagement between them on giving 6 months notice in advance. It is clarified that the Bank will be authorized to demand that the advance notice period will be actual employment, in whole or in part. In the advance notice period, the Chairman will be entitled to a salary and the rest of the related conditions.

If the Chairman's employment is terminated for any reason whatsoever (except in exceptional circumstances in which compensation may be denied the Chairman), the Chairman will be entitled to compensation amounting to 150% of the last salary times the number of years (and/or part thereof) of his term of office as Chairman of the Board of Directors, in addition to the Chairman's entitlement to the monies and rights accrued in the severance pay fund and provident fund. The Chairman gave an undertaking for a six-month cooling-off period, in which he is entitled to a salary and the rest of the related conditions. It is clarified that in a period in which the cooling-off period overlaps the advance notice period, in whole or part, the Chairman will be entitled only to payment in respect of the advance notice period.

The Remuneration Committee, the Board of Directors, and the General Meeting also confirmed (on 11 February 2014) that the Chairman of the Board of Directors is entitled to an annual performance-contingent bonus, pursuant to and subject to the provisions of the remuneration policy for office holders in the Bank as set forth in paragraph G. below, for each of the years 2013, 2014, 2015, and 2016.

Note 15 – Employee Rights (cont'd)

C. Details of provisions and amounts funded

Amounts of provisions and amounts funded for severance pay and pensions are included in the balance sheet as follows:

	31 December 2013	31 December 2012
	(NIS millions)	
Provision for severance pay	2,919	3,024
Amounts funded for severance pay (1)	(3,628)	(3,319)
Provision for pensions	5,644	5,096
Amounts funded for pensions	(182)	(174)
Excess of provisions over amounts funded, net	4,753	4,627
Excess of provisions over amounts funded, net, included in "other liabilities"	5,524	4,960
Excess of amounts funded included in "other assets"	771	333
Excess of provisions over amounts funded, net (2)	4,753	4,627

(1) The Bank and the consolidated companies may not withdraw amounts funded other than for the purpose of making severance payments.

(2) This surplus represents mainly the actuarial pension liability of the Bank for the pensioners of the Bank, and the cover for this liability is part of the Bank's assets and its current uses of funds.

Total liabilities for pensions to active employees who commenced work in the Bank before 1 January 1999 totaled NIS 7,489 million at 31 December 2013. To cover this liability, severance monies in the amount of NIS 2,465 million are deposited in Central Severance Pay Funds managed by a management company controlled by the Bank, as well as provident and severance monies deposited in a provident and severance fund in the amount of NIS 3,790 million which is managed by a management company owned by the members of the fund, as stated in paragraph F below. Provident monies are set off from pension liabilities and are not shown in the balance sheet and are also not detailed in the above table. The difference between the above provisions and amounts funded is provided for by the Bank and included under liabilities in the Bank's balance sheet.

Note 15 – Employee Rights (cont'd)

D. Long service bonuses

Employees of the Bank and some employees of consolidated companies are entitled, upon their attaining 20, 30 and 40 years of employment, to a monetary bonus in the amount of several monthly salaries ("jubilee grants") and to special vacation periods.

At the date of the balance sheet, there is a provision in the amount of NIS 691 million (31 December 2012 – NIS 678 million).

Calculation of the liability is made on an actuarial basis and takes into account, based on past experience, the probability that on the determining date, the employee will still be employed by the Bank. The said calculation is made using the capitalization rate published by the Supervisor of Banks (4%) and on the assumption of a real increase in salary based on past experience and varying in accordance with the age of the employee.

The provision for special service vacations is made on an actuarial basis taking into account past experience with respect to utilization of such vacations.

E. Provision for vacations

There is a provision of NIS 240 million under "Other Liabilities" for unutilized vacation pay (31 December 2012 - NIS 235 million). The provision is calculated on the basis of the latest salary plus related benefits.

F. Provident and severance pay funds of the employees of the Bank

The Bank deposits provident and severance monies for "first generation" employees in the Bank Leumi Employees Provident and Severance Funds, which is managed by a management company held by the members of the funds.

Until the end of 2012, the management company managed two provident and severance funds for Bank Leumi employees and Leumi Mortgage Bank employees. As of January 2013, the two funds were merged into one fund for all first generation employees.

The Bank provides the company with the services it requires to manage the fund, as permitted by law.

Commencing in 2008, the funds became non-pension payment provident funds, and provident monies funds cannot be withdrawn from these funds, unless they have been transferred to pension payment provident funds and subject to the conditions applying to the said funds.

In addition, as of 2011 the possibility of depositing monies in the Central Severance Pay Funds was restricted by law, and the Bank deposits severance monies in the provident fund in the name of the employees of the Bank.

G. Bonus Program for Senior Officers

On 11 February 2014, the General Meeting of the Bank, after obtaining the approval and recommendation of the Remuneration Committee and the approval of the Board of Directors, approved a remuneration policy regarding conditions of service and employment of Bank office holders (including senior office holders), pursuant to Amendment 20 of the Companies Law, 1999, pursuant to the directives of the Supervisor of Banks concerning remuneration policy of a banking corporation ("remuneration policy"), which includes a program for bonuses to office holders of the Bank (the

Note 15 – Employee Rights (cont'd)

"bonus program"). The remuneration policy and bonus program are valid for each of the years 2013, 2014, 2015, and 2016.

The bonus program provides, inter alia, the manner of determining the annual variable bonus for senior officers and the manner of determining the annual bonus for office holders who are not senior officers, the eligibility of the President and Chief Executive Officer to a fixed annual bonus, the eligibility of senior staff members in audit and control functions to a fixed annual bonus, and the possibility for the competent organs in the Bank to approve a signing-up bonus to a new office holder in the Bank; in accordance with the provisions of the remuneration policy as set out in a condensed form below:

1. The variable annual bonus to senior officers:

1.1. The variable annual bonus to senior officers is based, inter alia, on the rate of return on equity of the Bank, the Bank's annual performance relative to the objectives set by the Board of Directors and in relation to other banking groups, the performance of relevant units of the bank for measuring the performance of each senior officer, and on the development of the business results of the Bank over time.

1.2. The cumulative threshold conditions for variable annual bonus for senior officers are: (a) the employees of the Bank are entitled to a bonus for the relevant year; (b) the Bank achieved a minimum of 7.5% return on equity in the relevant year; and (c) the Bank met the capital adequacy ratios required under the directives of the Banking Supervision Department in the relevant year.

1.3. The variable annual bonus to senior officers is based on measurable criteria and qualitative criteria, as follows:

1.3.1. Part of the variable annual bonus based on measurable criteria shall be as specified below:

1.3.1.1. First, a basic annual variable bonus amount is to be determined for each of the senior officers in terms of fixed monthly remuneration amounts (employer's cost of one monthly amount), based on the rate of return on equity of the Bank for the bonus year and according to the role of each senior officers and his area of responsibility in the Bank and the Group (the "basic annual bonus"):

The basic annual bonus of the Chairman of the Board of Directors, the President and Chief Executive Officer, and senior officers not in audit and control functions (in a number of amounts of fixed monthly remuneration): 6 amounts for a rate of return on equity of 7.5%; 7 amounts for a rate of return on equity of 8%; 7.5 amounts for a rate of return on equity of 8.5%; 8 amounts for a rate of return on equity of 9%, 8.5 amounts for a rate of return on equity of 9.5%; 9 amounts for a rate of return on equity of 10%, 9.5 amounts for a rate of return on equity of 10.5%, and 10 amounts for a rate of return on equity of 11% and above.

The basic annual bonus for senior officers who belong to auditing and control functions in a number of amounts of fixed monthly remuneration): 4 amounts for a rate of return on equity of 7.5%; 4⅔ amounts for a rate of return on equity of 8%; 5 amounts for a rate of return on equity of 8.5%; 5⅓ amounts for a rate of return on equity of 9%, 5⅔ amounts for a rate of return on equity of 9.5%; 6 amounts

for a rate of return on equity of 10%, 6⅓ amounts for a rate of return on equity of 10.5%, and 6⅔ amounts for a rate of return on equity of 11% and above.
If the rate of return will be within a range of values listed above, the amount of the basic annual bonus will be determined for the relevant senior officer linearly between the two closest values.

1.3.1.2. After that, the basic annual bonus amount will be adjusted according to a measurable score of each senior officer from 80 to 120, with the measurable score each senior officer determined according to the following: (1) Twenty percent (20%) of the measurable score of each senior officer will be determined according to the comparison of return on equity in the bonus year versus the return on equity (weighted by shareholders' equity) in the four other major banks in Israel (Bank Hapoalim, Israel Discount Bank, Mizrahi – Tefahot Bank and the First International Bank) in that year; and (2) eighty percent (80%) of the measurable score of each senior officer will be determined according to a performance measurement sheet of the senior officer and the departments for which he is responsible, in the bonus year, less the return on equity of the Bank as a whole in the bonus year (this part of the measurable score of Chairman of the Board of Directors and the President and Chief Executive Officer, will be determined by a performance measurement sheet of the Bank as a whole).

1.3.2. Part of the variable annual bonus based on qualitative criteria shall be as specified as set forth below:

The Board of Directors, after receiving the recommendation of the President and Chief Executive Officer (other than with respect to the Chief Internal Auditor, for whom the recommendation will be given by the Audit Committee) and the approval of the Remuneration Committee will have the authority to approve an additional bonus amount as part of the variable annual bonus based on qualitative criteria in respect of the relevant year, for any of the senior officers in the Bank.

Part of this grant will be given to the senior officer subject to fulfillment of various qualitative criteria specified in the remuneration policy, in accordance with the areas of responsibility of the senior officer.

Subject to paragraph 1.4 below, the qualitative part of the bonus shall not constitute more than 20 % of the annual variable bonus of that officer senior in the relevant year.

1.4. Adjusting the basic annual bonus amount as stated in paragraph 1.3.1.2 above, plus the variable annual bonus based on qualitative criteria as stated in paragraph 1.3.2 above, may increase jointly the basic annual bonus by one and a half amounts of a fixed monthly remuneration.

1.5. The variable annual bonus amount for each of the above senior officers shall not in any event exceed 100% of the fixed annual remuneration of the senior officer (i.e. shall not exceed 12 monthly amounts of fixed annual remuneration), with the ratio of variable remuneration to fixed remuneration for senior officers who are members of audit and control functions, will incline more in favor of the fixed remuneration, in comparison with this ratio for other senior officers.

1.6. The checking of the variable annual bonus calculation for each senior officer will be made by an external expert, and then the calculated amount will be brought for approval of the Remuneration Committee and the Board of Directors.

1.7. The Board of Directors of the Bank, after receiving the approval of the Remuneration Committee, may decide, at its discretion, on a reduction in the variable annual bonus amount (in whole or in part) for senior officers in the Bank (all or some). For this purpose there will be taken into account, inter alia, Bank data in the bonus year and / or the years prior to the bonus year, relating to material profits of the Bank that the Board of Directors considers that they did not arise from normal activity, as well as material losses in those years.

1.8. If the variable annual bonus to the senior officer exceeded one sixth constant of his fixed annual remuneration, fifty percent (50%) of the variable annual bonus for that senior officer shall be paid in cash next following the reporting of the financial results of the banking system for the relevant year, and the remaining fifty percent (50%) will be awarded through blocked performance-contingent share units (PSU) to be allotted following the reporting of the financial results of the banking system for the relevant year, provided that the total amount and the accumulated PSU units to be allotted to all senior officers in the Bank for each year of the bonus program will not exceed 0.38% of the issued and paid up share capital of the Bank. If the amount of PSU units exceeded the said rate, the entitlement of all those eligible would be reduced by the same proportion to the said rate ceiling.

1.9. The PSU units will vest into ordinary shares of NIS 1 par value each of the Bank in three equal tranches (subject to that stated below) following the reporting of the financial results of the banking system of each of the three years after the bonus year, with the first amount of the three will be blocked for a period of one additional year. The vesting of the PSU share units will be contingent upon the fulfillment of two cumulative conditions: (a) rate of return on equity for the calendar year preceding the date of vesting of the relevant tranche of PSU units was not lower than 5%; and (b) The Bank complied with all the capital adequacy ratios required by the Supervisor of Banks according to the financial statements in the calendar year preceding the vesting date of the relevant tranche.

Allocating the PSU units and their conversion into shares of the Bank, shall be made in the capital gains track under Section 102 of the Income Tax Ordinance, as specified in the bonus program and subject to the approval of the Israel Tax Authority.

1.10. Retirement of a senior officer and joining of a new senior officer:

1.10.1. A senior officer retiring from the Bank after reaching the age of retirement or retiring from the Bank not on his own initiative during a calendar year shall be entitled to a proportional variable annual bonus for the actual term of office during the calendar year in which his resignation occurred, insofar as he is entitled to a variable annual bonus for that year.

Note 15 – Employee Rights (cont'd)

1.10.2. A senior officer retiring from the Bank voluntarily (not having reached retirement age) or was dismissed due to the occurrence of an event that allowed to be dismissed without compensation, during the calendar year, shall not be entitled to a variable annual bonus for the year of retirement.

1.10.3. A Bank employee who was promoted and appointed to the role of a senior officer in the Bank during a calendar year shall be entitled to a proportional variable annual bonus for the actual term of office during the calendar year in which the senior officer was appointed as aforesaid, insofar as he is entitled to a variable annual bonus for that year.

1.10.4. A person appointed to the role of a senior officer in the Bank during a calendar year, who was not previously an employee of the Bank, is entitled to a proportional variable annual bonus for the actual term of office in the year of appointment, insofar as he is entitled to a variable annual bonus for that year.

1.11. Special bonus: in accordance with the provisions of paragraph 13(a)(2) of Proper Conduct of Banking Business Directive 301A, in exceptional and outstanding cases, the Remuneration Committee and the Board of Directors will be entitled, and when required by the Companies Act after receiving the approval of the General Meeting, as applicable, to approve the amount of an additional variable bonus in respect of a given year for some of its officers, subject to the following conditions: (1) The additional variable bonus will be given due to an exceptional event not recurring every year, such as a one – time project, a material structural change and / or an extraordinary transaction in scope and essence, provided that the exceptional business event was defined in advance by the Board of Directors at the beginning of the year relevant to the specific office holder. Accordingly, the Board of Directors decided on the said events and projects for 2014, and on measurable criteria for determining the above special bonus. (2) The total maximum variable remuneration for an office holder in the same year shall not exceed 200% of the fixed annual remuneration of that senior officer. (3) Detailed reasons will be given for the relevant decision, when a decision is made.

2. Fixed annual payment to the President and Chief Executive Officer: the President and Chief Executive Officer will be entitled to a fixed annual bonus of one amount of fixed monthly remuneration. The fixed annual bonus of the President and Chief Executive Officer is part of the calculation of the "fixed monthly remuneration" used for calculating the variable annual bonus of the President and Chief Executive Officer.

3. Fixed payment to senior officers who are members of the audit and control functions: senior officers in the audit and control functions will be entitled to a fixed annual bonus of one amount of fixed monthly remuneration. Without detracting from this bonus being part of the fixed remuneration component of the senior officers in the audit and control functions, this bonus will not be part of the calculation of the "fixed monthly remuneration" used for calculating the variable annual bonus of the senior officers.

4. Signing-up bonus for a new office holder: a new office holder of the Bank may be entitled to a limited signing-up bonus for the first year of work, up to 12 amounts of fixed monthly remuneration. The Remuneration Committee followed by the Board of Directors will consider, for the purpose of making the decision on granting the said signing-up bonus and its amount, the recommendation of the President and Chief Executive Officer, and will consider for this purpose, inter alia, the circumstances of his appointment, the nature of the job to which he is appointed, the scope and areas of his responsibility, and so forth.

5. Notwithstanding the aforesaid and in accordance with the Companies Law, an office holder will return to the Bank amounts of bonuses paid to him, if paid to him, on the basis of data found to be erroneous and restated in the financial statements of the Bank.

6. Bonuses, insofar as the office holders will be eligible for bonuses under this program, will not be taken into account for social contributions, severance, and retirement pension and will not be considered as a fringe benefit of any kind for any of the office holders.

Appropriate provisions have been made in the financial statements.

H. Sale of Shares to Employees

In accordance with the agreements concerning the privatization of the Bank, and in accordance with agreements reached between the Accountant-General in the Finance Ministry and the employees of the Bank, an outline prospectus was published on 6 April 2011 for the offer by the State of Israel of the Bank's shares to employees of the Bank, Arab-Israel Bank Ltd., Leumi Mortgage Bank Ltd., and the Restaurant Association of Employees of Bank Le-Israel B.M. (registered association) ("the participants", "the outline prospectus").

On 17 May 2011, the purchase was completed by the participants, in accordance with and subject to arrangements and conditions detailed in the outline prospectus, of 6,339,730 shares held by the State of Israel representing 0.43% of the Bank's issued and paid-up share capital of the Bank, as at the date of publication of the outline prospectus. On 24 May 2011, the General Meeting of the Bank approved the offer of 9,442 shares to the Chairman of the Board of Directors of the Bank, and the grant of a loan by the Bank to purchase the shares. On 30 May 2011, the Bank was informed by the Ministry of Finance that on 29 May 2011, the sale of the shares to the Chairman of the Board of Directors was completed.

The price per share for purposes of the offer to participants according to the outline prospectus was NIS 13.20825 per share as at 19 January 2011, and this share price was linked to the Consumer Price Index using the "last known index" method, with the base index being the index for the month of December 2010, that was published on 14 January 2011.

The share price was NIS 13.3002797 (The price of the shares purchased by the Chairman of the Board of Directors was NIS 13.37813).

The allocation of shares to the participants and the determination of the number of shares offered each participant, was made relative to the salary serving as a basis for social provisions for those participants for the month of January 2011, in accordance with the terms of the outline prospectus. The Chairman of the Board (as stated above) and the President and CEO of the Bank are included in the participants.

The shares are blocked for a period of four years from the determining date (as defined in the outline prospectus), and are deposited with a trustee.

In addition, the Audit Committee and the Board of Directors approved the granting of loans to the participants for the purchase of the shares offered in the outline prospectus.

The value of the benefit to the employees and to the Chairman of the Board of Directors in respect of the aforesaid purchase, which was assessed by an external valuer, includes a number of components, and amounts to some NIS 13 million. This amount was recorded as a salary expense in accordance with the value of the benefit on the day it was granted and this amount remains fixed. A benefit of NIS 13 million was recorded in a capital reserve.

To finance the purchase of the shares, the Bank extended loans to the employees amounting to some NIS 43 million, with repayment in one amount at the end of the blocked period of the shares, of which loans amounting to NIS 12 million are linked to the Consumer Price Index, bearing interest at 1.55%, and loans amounting to NIS 31 million are unlinked based on the Prime rate less 0.75%. The loans are not under non-recourse conditions. The amount of the loans was deducted from the Bank's capital.

I. Streamlining – Structural change

In 2013 and in 2012, expenses were recorded of about NIS 75 million and NIS 323 million (respectively) for bringing forward the retirement of employees under the program for reducing manpower in the Bank pursuant to the plan for structural change in the Bank. This program is spread over the years 2012-2014.

J. Effect of the change in the rate of tax

For information regarding the effect of the change in tax rates on the liabilities for employee rights, see Note 26 below.

Note 16 - Assets and Liabilities by Linkage Basis

	31 December 2013						
	Israeli currency		Foreign currency (1)				
	Unlinked	Linked to the CPI	In U.S. dollars	In Euro	In other currencies	Non-monetary items (2)	Total
	NIS millions						
Assets							
Cash and deposits with banks	29,847	272	6,667	2,475	4,964	126	44,351
Securities	34,323	3,410	16,506	3,745	1,832	3,919	63,735
Securities borrowed or purchased under agreements to resell	1,350	-	-	10	-	-	1,360
Credit to the public, net (3)	146,545	53,544	27,213	6,020	7,190	362	240,874
Credit to governments	65	273	176	44	-	-	558
Investments in companies included on equity basis	-	-	-	-	-	1,689	1,689
Buildings and equipment	-	-	-	-	-	3,638	3,638
Assets in respect of derivative instruments	8,678	309	2,076	347	202	1,442	13,054
Other assets and intangible property	3,684	4	922	7	126	358	5,101
Total assets	224,492	57,812	53,560	12,648	14,314	11,534	374,360
Liabilities							
Deposits of the public	154,825	28,779	74,139	16,883	10,756	621	286,003
Deposits from banks	1,717	117	1,840	523	113	-	4,310
Deposits from governments	24	3	360	10	-	-	397
Securities loaned or sold under agreements to repurchase	624	-	-	-	-	-	624
Debentures, bonds and subordinated notes	4,554	20,877	-	-	10	-	25,441
Liabilities in respect of derivative instruments	8,362	514	2,054	835	269	1,453	13,487
Other liabilities	9,561	5,840	1,028	25	269	610	17,333
Total liabilities	179,667	56,130	79,421	18,276	11,417	2,684	347,595
Difference (4)	44,825	1,682	(25,861)	(5,628)	2,897	8,850	26,765
Effect of hedging derivative instruments							
Derivative instruments (except options)	694	-	-	-	(694)	-	-
Options in the money, net (in terms of underlying asset)	-	-	-	-	-	-	-
Options out of the money, net (in terms of underlying asset)	-	-	-	-	-	-	-
Effect of non-hedging derivative instruments:	-	-	-	-	-	-	-
Derivative instruments (except options)	(25,740)	(2,441)	25,700	5,460	(2,629)	(350)	-
Options in the money, net (in terms of underlying asset)	1,125	-	(1,127)	(43)	36	9	-
Options out of the money, net (in terms of underlying asset)	876	-	(1,284)	462	(59)	5	-
Total	21,780	(759)	(2,572)	251	(449)	8,514	26,765
Effect of non-hedging derivative instruments:							
Options in the money, net (discounted par value)	1,226	-	(1,279)	25	16	12	-
Options out of the money, net (discounted par value)	4,252	-	(3,947)	65	(428)	58	-

See notes on next page.

Note 16 - Assets and Liabilities by Linkage Basis (cont'd)

	31 December 2012						
	Israeli currency		Foreign currency (1)				
	Unlinked	Linked to the CPI	In U.S. dollars	In Euro	In other currencies	Non-monetary items (2)	Total
	(NIS millions)						
Assets							
Cash and deposits with banks	39,306	277	8,971	1,686	4,154	227	54,621
Securities	27,179	4,761	16,249	3,976	1,877	2,366	56,408
	-	-	-	-	-	-	-
Securities borrowed or purchased under agreements to resell	1,435	-	-	-	-	-	1,435
Credit to the public, net (3)	137,700	54,847	32,924	6,622	9,077	94	241,264
Credit to governments	13	269	124	36	-	-	442
Investments in companies included on equity basis	-	-	-	-	-	2,129	2,129
Buildings and equipment	-	-	-	-	-	3,705	3,705
Assets in respect of derivative instruments (5)	7,538	184	2,938	260	168	350	11,438
Other assets and intangible property	2,849	3	893	8	178	787	4,718
Total assets	216,020	60,341	62,099	12,588	15,454	9,658	376,160
Liabilities							
Deposits of the public	151,962	28,467	79,894	17,620	11,257	338	289,538
Deposits from banks	1,694	166	1,765	318	130	-	4,073
Deposits from governments	15	109	319	8	-	-	451
Securities loaned or sold under repurchase agreements	951	-	56	-	-	-	1,007
Debentures, bonds and subordinated notes	6,301	21,214	-	-	10	-	27,525
Liabilities in respect of derivative instruments (5)	7,973	561	3,091	593	230	314	12,762
Other liabilities	8,553	5,330	629	28	285	751	15,576
Total liabilities	177,449	55,847	85,754	18,567	11,912	1,403	350,932
Difference (4)	38,571	4,494	(23,655)	(5,979)	3,542	8,255	25,228
Effect of hedging derivative instruments							
Derivative instruments (except options)	746	-	-	-	(746)	-	-
Options in the money, net (in terms of underlying asset)	-	-	-	-	-	-	-
Options out of the money, net (in terms of underlying asset)	-	-	-	-	-	-	-
Effect of non-hedging derivative instruments:							
Derivative instruments (except options) (5)	(19,170)	(6,280)	22,507	6,687	(3,744)	-	-
Options in the money, net (in terms of underlying asset)	(431)	-	231	5	195	-	-
Options out of the money, net (in terms of underlying asset)	(133)	-	284	(146)	(5)	-	-
Total	19,583	(1,786)	(633)	567	(758)	8,255	25,228
Effect of non-hedging derivative instruments:							
Options in the money, net (discounted par value)	(575)	-	273	(20)	322	-	-
Options out of the money, net (discounted par value)	(1,630)	-	2,042	(436)	24	-	-

(1) Including linked to foreign currency.
(2) Including derivative instruments whose underlying asset is a non-monetary item.
(3) After deduction of credit loss allowances attributable to linkage bases in the amount of NIS 3,883 million (31 December 2012 – NIS 4,114 million)..
(4) Shareholders' equity includes non-controlling interests.
(5) Reclassified.

Note 17 - Assets and Liabilities by Currency and Repayment Date (1)

	31 December 2013													
	Estimated future contractual cash flows											Book balance (4)		
	Upon demand and up to one month (6)	One month to three months (6)	Three months to one year (6)	One year to two years	Two years to three years	Three years to four years	Four years to five years	Five years to ten years	Ten years to twenty years	Over twenty years	Total cash flows	Without fixed maturity (2)	Total	Contractual rate of return (5) in %
	(NIS millions)													
Israeli currency (including linked to foreign currency):														
Assets	68,498	20,545	62,469	28,485	21,445	17,424	13,446	40,876	34,336	11,361	318,885	2,995	282,679	3.67
Liabilities	136,867	14,960	30,151	16,892	9,740	11,267	3,225	15,214	3,198	2,406	243,920	2,271	238,703	2.37
Difference	(68,369)	5,585	32,318	11,593	11,705	6,157	10,221	25,662	31,138	8,955	74,965	724	43,976	
Derivative instruments (except options)	(10,197)	(12,755)	(2,147)	(488)	172	(117)	18	171	(27)	(78)	(25,448)	-	(25,515)	
Options (in terms of underlying asset)	779	(372)	20	15	-	-	162	1,399	-	-	2,003	-	1,902	
Difference after effect of derivative instruments	(77,787)	(7,542)	30,191	11,120	11,877	6,040	10,401	27,232	31,111	8,877	51,520	724	20,363	
Foreign currency (3)														
Assets	26,057	7,231	12,840	10,020	6,854	6,227	5,911	8,525	2,189	487	86,341	473	80,147	3.85
Liabilities[9]	71,680	13,524	15,106	2,747	1,071	998	2,076	1,321	374	4	108,901	517	106,208	3.06
Differenc	(45,623)	(6,293)	(2,266)	7,273	5,783	5,229	3,835	7,204	1,815	483	(22,560)	(44)	(26,061)	
Of which difference in $	(40,772)	(895)	(2,615)	5,980	4,204	3,739	1,958	5,521	1,368	368	(21,144)	(111)	(24,174)	
Of which: difference in respect of foreign operations	(3,076)	(1,145)	(1,084)	(2,654)	(1,184)	(5,195)	(64)	(3,644)	258	73	(17,715)	(172)	(16,075)	
Derivative instruments (except options)	10,197	12,755	2,147	488	(172)	117	(18)	(171)	27	78	25,448	-	25,515	
Options (in terms of underlying asset)	(779)	372	(20)	(15)	-	-	(162)	(1,399)	-	-	(2,003)	-	(1,902)	
Difference after effect of derivative instruments	(36,205)	6,834	(139)	7,746	5,611	5,346	3,655	5,634	1,842	561	885	(44)	(2,448)	
Total														
Assets[8]	94,555	27,776	75,309	38,505	28,299	23,651	19,357	49,401	36,525	11,848	405,226	3,468	362,826	3.70
Liabilities[9]	208,547	28,484	45,257	19,639	10,811	12,265	5,301	16,535	3,572	2,410	352,821	2,788	344,911	2.58
Difference (7)	(113,992)	(708)	30,052	18,866	17,488	11,386	14,056	32,866	32,953	9,438	52,405	680	17,915	
[8]Of which: credit to the public	47,037	24,207	44,293	29,499	21,517	17,187	12,950	37,811	33,531	11,467	279,499	1,234	240,512	3.99
[9]Of which: deposits of the public	197,704	24,037	37,968	10,175	5,088	3,330	3,984	5,198	737	8	288,230	-	285,382	1.92

See notes on next page.

Note 17 - Assets and Liabilities by Currency and Repayment Date [1] (cont'd)

	31 December 2012													
	Estimated future contractual cash flows											Book balance [4]		
	Upon demand and up to one month (6)	One month to three months (6)	Three months to one year (6)	One year to two years	Two years to three years	Three years to four years	Four years to five years	Five years to ten years	Ten years to twenty years	Over twenty years	Total cash flows	Without fixed maturity (2)	Total	Contractual rate of return (5) in %
	(NIS millions)													
Israeli currency (including linked to foreign currency):														
Assets	78,551	20,678	52,447	32,958	20,475	14,838	14,019	37,666	29,751	10,263	311,646	1,961	277,099	3.54
Liabilities	127,804	14,522	34,945	15,665	11,474	7,597	10,363	15,720	3,178	1,895	243,163	2,459	234,382	2.66
Difference	(49,253)	6,156	17,502	17,293	9,001	7,241	3,656	21,946	26,573	8,368	68,483	(498)	42,717	
Derivative instruments (except options)	(2,593)	(11,459)	(9,642)	(264)	(318)	(314)	216	135	(406)	(86)	(24,731)	-	(24,704)	
Options (in terms of underlying asset)	(505)	(327)	271	(7)	9	-	-	-	-	-	(559)	-	(564)	
Difference after effect of derivative instruments	(52,351)	(5,630)	8,131	17,022	8,692	6,927	3,872	22,081	26,167	8,282	43,193	(498)	17,449	
Foreign currency (3)														
Assets	29,790	8,175	16,976	11,108	7,746	7,091	4,352	6,394	1,891	367	93,890	348	89,403	2.74
Liabilities	68,965	17,730	21,127	2,875	1,217	896	2,714	837	72	5	116,438	65	115,147	2.51
Difference	(39,175)	(9,555)	(4,151)	8,233	6,529	6,195	1,638	5,557	1,819	362	(22,548)	283	(25,744)	
Of which difference in $	(27,354)	(2,410)	(4,402)	4,264	694	1,454	2,511	2,867	482	198	(21,696)	366	(20,863)	
Of which: difference in respect of foreign operations	(4,489)	38	(2,230)	(309)	(1,884)	(1,471)	(7,342)	(4,126)	480	93	(21,240)	110	(18,493)	
Derivative instruments (except options)	2,593	11,459	9,642	264	318	314	(216)	(135)	406	86	24,731	-	24,704	
Options (in terms of underlying asset)	505	327	(271)	7	(9)	-	-	-	-	-	559	-	564	
Difference after effect of derivative instruments	(36,077)	2,231	5,220	8,504	6,838	6,509	1,422	5,422	2,225	448	2,742	283	(476)	
Total														
Assets[8]	108,341	28,853	69,423	44,066	28,221	21,929	18,371	44,060	31,642	10,630	405,536	2,309	366,502	3.42
Liabilities[9]	196,769	32,252	56,072	18,540	12,691	8,493	13,077	16,557	3,250	1,900	359,601	2,524	349,529	2.64
Difference (7)	(88,428)	(3,399)	13,351	25,526	15,530	13,436	5,294	27,503	28,392	8,730	45,935	(215)	16,973	
[8]Of which: credit to the public	51,176	24,545	45,227	30,902	21,360	15,810	12,908	35,559	29,085	9,875	276,447	1,385	241,170	3.79
[9]Of which: deposits of the public	172,967	26,186	45,900	12,650	7,581	5,399	9,514	8,425	695	7	289,324	-	289,200	1.26

See notes on next page.

Note 17 - Assets and Liabilities by Currency and Repayment Date [1] (cont'd)

Notes:

(1) In this Note, forecast contractual future cash flows in respect of assets and liabilities are shown according to linkage basis, in accordance with the remaining contractual period to maturity of each cash flow. The data is presented after deduction of allowance for credit losses.

(2) Assets without a fixed maturity include assets in the amount of NIS 514 million that are overdue.

(3) Not including Israeli currency linked to foreign currency.

(4) As included in Note 16, "Assets and Liabilities According to Linkage Basis", including off-balance sheet amounts in respect of derivatives that are not settled net.

(5) The contractual rate of return is the interest rate discounting future anticipated contractual cash flows reported in this Note in respect of a monetary item to the balance sheet figure.

(6) Credit with revolving account conditions is classified in accordance with the period of the credit facility in the amount of NIS 13.0 billion (31 December 2012 - NIS 12.1 billion). Over-limit credit in the amount of NIS 0.7 billion (31 December 2012 - NIS 0.4 billion) is classified as without repayment date.

(7) The above difference does not necessarily reflect the exposure to interest and/or linkage basis.

Note: Total memorandum liabilities against which short-term credit was granted in the Bank amount to NIS 5.1 billion as of 31 December 2013 (31 December 2012 - NIS 4.5 billion).

Note 18 - Contingent Liabilities and Special Commitments

	31 December 2013		31 December 2012	
	Contract balances	Balance of allowance for credit losses	Contract balances	Balance of allowance for credit losses
	(NIS millions)			
A. Off-balance sheet financial instruments				
Balances of contracts or their stated amounts as at the end of the period				
Transactions in which the balance reflects a credit risk:				
Documentary credits	**1,867**	**4**	1,823	5
Credit guarantees	**5,490**	**84**	5,793	76
Guarantees to apartment purchasers	**15,529**	**22**	13,538	18
Other guarantees and liabilities	**15,033**	**172**	16,504	221
Unutilized credit card facilities	**24,669**	**22**	22,582	21
Other unutilized revolving credit facilities and credit facilities in accounts on demand	**14,158**	**24**	14,434	31
Irrevocable commitments to provide credit which has been approved and not yet granted[1]	**20,801**	**66**	20,892	60
Commitments to issue guarantees	**11,845**	**18**	10,818	15
Unutilized facilities for activity in derivative instruments	**6,406**	**-**	6,129	-
Approval in principle for a guaranteed rate of interest	**3,692**	**-**	3,689	-

[1]Of which: credit exposures in respect of the obligation to provide liquidity to securitization structures under the auspices of others not utilized in the amount of NIS 208 million (31 December 2012 – NIS 224 million). This commitment is only made in a situation where financing difficulties do not facilitate securitization. Currently and in the past the liquidity facility was not utilized. The lines provided by the Bank represent a small part of the overall volume of liquidity lines provided to those entities. The Bank does not provide these entities with any other kind of support.

	31 December 2013	31 December 2012
	(NIS millions)	
B. Off-balance sheet commitments for transactions based on extent of collections (1)		
Balance of credit from deposits based on extent of collections (2)		
Israeli currency unlinked	**1,070**	1,160
Israeli currency linked to the CPI	**3,785**	4,493
Foreign currency	**267**	410
Total	**5,122**	6,063

See notes on next page.

Note 18 - Contingent Liabilities and Special Commitments (cont'd)

Cash flows in respect of collection commissions and interest margins on activities based on the extent of collections as at December 31

	Up to one year	One to three years	Three to five years	Five to ten years	Ten to twenty years	More than twenty years	Total 2013	Total 2012
	(NIS millions)							
(1) CPI linked sector (3)								
Cash flows of futures contracts	75	39	38	67	24	1	244	242
Expected future cash flows after management estimate of early repayments	75	39	38	67	23	-	242	240
Discounted expected future cash flows after management estimate of early repayments (4)	75	37	33	54	16	-	215	207
(2) Unlinked shekel sector								
Cash flows of futures contracts	4	4	3	5	1	-	17	19
Expected future cash flows after management estimate of early repayments	4	4	3	5	1	-	17	19
Discounted expected future cash flows after management estimate of early repayments (4)	4	4	3	4	-	-	15	17

(1) Credit and deposits out of deposits returnable upon repayment of the credit (or the deposits) with interest margin or with collection commission (instead of interest margin).

(2) Standing loans and Government deposits given in respect thereof in the amount of NIS 267 million (previous year - NIS 327 million) are not included in this table.

(3) Including foreign currency sector.

(4) Discounting was at the rate of 2.97% (2012 – at the rate of 2.69%).

Note 18 - Contingent Liabilities and Special Commitments (cont'd)

	2013	2012
	(NIS millions)	
B. Off-balance sheet commitments for activity based on extent of collection (cont'd)		
Information on loans granted during the year by mortgage banks:		
Loans from deposits on collection basis	**38**	34
Standing loans	**28**	15
C. Other contingent liabilities and special commitments:		
(1) Long-term rental contracts - rental of buildings, equipment and motor vehicles and maintenance in respect of commitments payable in following years		
First year	**225**	270
Second year	**195**	198
Third year	**174**	182
Fourth year	**162**	165
Fifth year	**130**	132
After five years	**815**	846
Total	**1,701**	1,793
(2) Commitments to purchase securities	**568**	531
(3) Commitments to invest in and acquire buildings and equipment	**56**	217
(4) Future deposits		
Transactions with depositors for purposes of receipt of large deposits at various future dates and at fixed interest rates determined in advance as of the date of the commitment.		
Details of amounts of future deposits and deposit dates as determined in the terms of the transactions:		
First year	**17**	17
Second year	**12**	17
Third year	**3**	12
Fourth year	**-**	3
Total future deposits	**32**	49

Note 18 - Contingent Liabilities and Special Commitments (cont'd)

D. In the 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 success of the claims, 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, each of which exceeding NIS 2 million, and regarding which the chances of the claims succeeding are not remote, amounts to some NIS 92 million.

1. The following are details of claims in material amounts in excess of 0.5% of the equity of the Bank at 31 December 2013 (about NIS 132 million):

A. 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 claimant group amounts to NIS 10 billion. No specific sum of the amount of the claim has been clearly attributed to any of the respondents. 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 a prohibited restrictive arrangement. On 21 January 2008, the Tel Aviv District Court approved the pursuance of the claim as a class action. The Banks submitted an appeal against the ruling in the Supreme Court. In the context of the hearing of the appeal, the Attorney General submitted, on 21 November 2011, his position dealing with the implications of the decision by the Anti-Trust Commissioner dated 26 April 2009, under the heading "Restrictive Arrangements between Bank Hapoalim, Bank Leumi, Bank Discount, Bank Mizrahi, and the First International Bank, concerning the Transfer of Information relating to Commissions" ("the decision"). The essence of this position is that in the view of the Attorney General the decision justifies the approval of a class action. It should be noted that in the appeal proceedings the Attorney General also referred to the decision in his previous position of May 2010, where it stated that this decision refers to commissions, whereas the decision of the District Court deals with interest rates. On 28 July 2013, the Supreme Court decided to accept the appeal and the decision of the District Court to approve a class action was canceled. The Supreme Court also decided that in view of the fact that the decision may have significant implications on the approval of the class action, there is no alternative than to return the proceedings to the District Court for a further hearing on the petition for approval.

B. 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 of credit to the household sector, the banks collect interest at a rate that is much higher than that collected from the commercial sector and from the corporate sector. The petitioners claim that this is exploitation of monopolistic power and that there is a real concern that the lack of competition between the respondents, regarding all matters concerning the households sector, is the result of a restrictive arrangement between the parties. It is also alleged that this is misleading consumers regarding the normal price for credit service to the household.

Note 18 - Contingent Liabilities and Special Commitments (cont'd)

The alleged damage 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 District Court granted a stay of these proceedings in this request 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 A. above. The plaintiffs submitted a petition, on 29 October 2013, for renewal of proceedings in the claim. The decision of the Court on the petition to renew proceedings has not yet been handed down.

C. On 3 January 2008, 260 identical claims were filed in the Tel Aviv-Jaffa Magistrates' Court against the Bank and receivers who had been appointed by the court. The amount of the claims ranges from some NIS 787,000 to some NIS 1,350,000. Pursuant to the Court's ruling, the proceedings for all of the abovementioned claims were combined, and they will be heard as one claim. The aggregate amount of the claims is some NIS 276 million. The plaintiffs are the purchasers of vacation apartments in the Nofit Hotel project in Eilat. According to the plaintiffs, the Bank and the receivers were negligent in supervising the project and refrained from financing the guarding fees, 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 were filed against the Bank on the same grounds, and 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 abovementioned 260 claims. The plaintiffs appealed the ruling. The court ordered a stay of proceedings in the claims until a judgment had been given in the appeal submitted on the aforesaid ruling. On 17 June 2010, the appeal was dismissed, and following this, the Bank filed a petition to dismiss the aforesaid 260 claims. On 20 June 2010, the Court handed down a decision which determined that there were grounds for dismissing the claims, and requested the parties' response. The plaintiffs have notified the court of their desire to continue the proceedings. The plaintiffs filed petitions to amend the claims, and the Bank filed a petition to dismiss the claims outright under the finality of judgment rule. On 14 May 2012, the Court found in favor of the petition of the Bank and rejected the claim outright. The plaintiffs filed an appeal against the verdict in the District Court. On 11 March 2014, a verdict was handed down rejecting most of the appeal, and accepting the Bank's clasims in full regarding rejection outright due to a final judgment. However, the Court returned the case to the Magistrates Court to examine whether to allow filing an amended claim on the grounds that there was no final judgment.

D. 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 said 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 were not), 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, and the provisions of the Execution Law. 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. On 15 November 2009, the District Court gave an order postponing the execution of its decision for approval of the claim as a class action, until the decision of the Supreme Court in the petition for leave of appeal against the said decision, filed by the Bank on 18 November 2009. On 27 July 2011, the Bank's petition to grant leave of appeal against the decision of the District Court approving the claim as a class action was dismissed in the Supreme Court, and hearings in the claim were returned to the District Court. After the signing of an arrangement between the parties to resolve the claim, the Court, on 9 June 2013, appointed an examiner for the compromise arrangement and ordered publication of a notice regarding the arrangement.

E. On 29 October 2009, a claim for declaratory judgments was filed in the Central District Court to the effect, *inter alia*, 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 2003 and thereafter. 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 determined 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%. On 11 February 2010, a monetary claim of NIS 829 million was submitted, to replace the claim for declaratory judgments that was dismissed. A statement of defense was submitted, preliminary statements of testimony were submitted; evidence was heard in the claim and summaries submitted. On 21 July 2013, a verdict was handed down accepting the claim on a partial basis only. Within 30 days of the handing down of the verdict, an interest calculation will be made in accordance with the rate decided in the verdict. The plaintiffs submitted their own calculation to the court and the banks submitted their response to the calculation. The parties are awaiting a final verdict. On 7 November 2013, a temporary order was granted deferring the carrying out of the verdict. The parties have filed an appeal to the Supreme Court.

F. On 3 May 2010, a petition for approval of a class action was filed in the Central District Court claiming an amount of some NIS 209 million as of the date the claim was filed. The plaintiff is interested in representing all those holding debentures of Heftziba Hofim Ltd. ("Heftziba Hofim"), prior to the suspension of their trading at the beginning of August 2007. The petitioner claims that during the years 2006-2007, prior to the end of each quarter, the Bank granted loans in amounts of tens of millions of shekels to a company wholly owned by Mr. Boaz Yonah. According to the petitioner's claim, these funds were transferred for a short period of time to the account of Heftziba Hofim, and helped it to make momentary false presentations to the public regarding its true financial condition. The petitioner claims that as a result of cooperation by the Bank and the false representations made to the public, the investments of those holding debentures of Heftziba Hofim were eventually written off. The Bank's response has been filed to the petition for approval of the claim as a class action. On 20 October 2013, the parties filed a petition with the court for approval of a compromise arrangement in the case. The arrangement has not yet been approved by the court.

G. On 13 July 2011, a petition was filed in the Tel-Aviv District Court for approval of a class action against Automatic Bank Services Ltd. (hereinafter: "ABS") and against Bank Hapoalim B.M., Bank Leumi Le-Israel B.M., First International Bank of Israel B.M., and Israel Discount Bank B.M. ABS is a service company jointly owned by the banks mentioned above, whose activities include operating an independent network of automatic teller machines (ATM). It is claimed in the petition that when withdrawing cash from an ATM operated by ABS, the user is not provided with fair disclosure that in addition to the commission charged by ABS for the withdrawal, he will be charged additional commission by the bank in which his account is held. In addition, it is claimed in the petition that the banks are not authorized to charge their customers additional commission, after they were already charged for the withdrawal by ABS. The total amount claimed in the class action, in the opinion of the petitioners, is NIS 153.3 million, with the addition of linkage differentials and interest. There are no details of the distribution between the defendants. Mediation proceedings are taking place between some of the parties.

H. On 7 September 2011, a petition for approval of a class action was filed against the Bank (formerly Leumi Mortgage Bank), Mizrahi Tefahot Bank Ltd. and Bank Hapoalim B.M. The amount of the class action claimed against all the respondent banks is approximately NIS 927 million as at 1 January 2010, and the amount of the class action against the Bank is about NIS 327 million. The petitioners claim that the respondent banks charged housing-loan borrowers "compound interest in advance", contrary to the law and to the loan agreements, which stipulate that only the unpaid balance of principal will bear interest. The reliefs claimed are payment of compensation and/or reinstatement of damage caused to borrowers and the amounts charged unlawfully, and the granting of a court order against the respondent banks to change the way they act in all areas related to charging and collecting interest. The Bank filed its response to the petition with the Court. In a preliminary hearing in the claim on 16 October 2012, the Court requested the Supervisor of Banks to address several questions that arose in the opinion of each of the parties to the claim. In accordance with the request of the Court, the Bank of Israel submitted its responses to the questions raised by the parties concerning the claim on 31 December 2012.

I. On October 11, 2012, a claim and petition for approval of a class action was filed in the Tel Aviv District Court against Leumi, First International, Mizrahi-Tefahot and Israel Discount Bank. The plaintiffs claim that the bank accounts of the Bank's customers against whom collection proceedings are being conducted, and who made payments directly to files in the Execution Office, were updated at a date later than the date of payment. Due to the delay in updating payments in the bank account, the plaintiffs were charged excessive interest charges. The plaintiffs claim that the entry in the bank account is important for the client, and payment should not be made with value two days later. The remedies requested in the claim and petition are: the refund of excess amounts paid by customers, injunctions and declarative orders for updating payments in the accounts, from now on, with value of the date the amounts were actually made to the Execution Office, and the amendment of accounts still under proceedings, in accordance with the correct value dates. According to the plaintiffs, the amount of the class action cannot be estimated at this time.

2. In addition, there are legal claims pending against the Bank, including petitions for the 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.

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 and Bank Hapoalim, (hereinafter: “the Banks”). It is claimed that the Banks had 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 unlawfully enriched themselves at the expense of their customers. It is claimed, as an estimate, that had the rates not been coordinated between the Banks, the commissions would have been significantly lower, by at least 25%. The total aggregate amount of the damage is estimated in the amount of NIS 3.5 billion, with the heading of the petition indicating the amount of the claim as NIS 3 billion. No specific attribution has been made of the damage claimed from 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. The hearing in this file was incorporated with a later claim (see description in paragraph B. below). On 29 November 2009, the Court decided to stay proceedings in the claim for two years (subject to the provisions set out in that decision) in view of the respondents' intention to submit a petition for leave to appeal the Commissioner’s determination of 26 April 2009 in the Restrictive Practices Court. On 23 February 2012, the Court decided to continue the stay of proceedings until the decision of the Restrictive Practices Court on the appeal filed against the Commissioner's determination. On 29 October 2013, the plaintiffs filed a petition for renewal of proceedings in the claim. The decision of the Court on the petition to renew proceedings has not yet been handed down.

B. 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 Tefahot Bank and the First International Bank. The petition is based on the Antitrust Commissioner’s determination of 26 April 2009. The petitioners allege that in accordance with the determination, the banks made restrictive arrangements for the exchange of information on commissions, to the detriment of competition between them, and which caused damage to the members of the group whose representation is sought in the petition, and that such was reflected in overpayments of commissions. The petitioners estimate the amount of the class action against all the respondents at NIS 1 billion. The petition does not make any clear attribution of a specific claimed amount to each of the respondents. Proceedings in the petition for approval have been stayed for two years, as stated in the decision of 29 November 2009, described in paragraph A. above. On 23 February 2012, the Court decided to continue the stay of proceedings until the decision of the Restrictive Practices Court on the appeal filed against the Commissioner's determination. An additional petition for renewal of proceedings was heard in the Court and a further date for the hearing was set, in the framework of which the respondents will be required to update the Court as to progress in the above appeal proceedings.

C. On 28 August 2013, a petition was filed with the Tel Aviv District Court to approve a class action against Bank Hapoalim, Bank Leumi, Bank Mizrahi-Tefahot, Israel Discount Bank, First International Bank, and the CEO's of these banks. The Supervisor of Banks, the

Governor of the Bank of Israel, and the Antitrust Commissioner were joined as formal respondents. The subject of the petition is the unlawful charging of commissions regarding activities of conversion and delivery of foreign currency, without fair disclosure. According to the petitioners, the banks are concealing from the customers that, when selling / buying foreign currency, they are also charged in excess of exchange commission, as defined by them, a "price increase" or "price reduction" commission – i.e. exchange rate differences. They argue that the disclosure made by the banks at the time of the transaction refers only to exchange commission and not to exchange rate differences. They argue that since the bank is a Forex "intermediary" and not a "market maker", it should charge customers the price it was charged for the foreign currency, perhaps with a miniscule addition, and in any case it should disclose this to the customer. As claimed by the petitioners, the direct damage caused to customers is at least NIS 10.5 billion over the last seven years, subject to documents and information they will receive as part of the claim. Following submission of the petition for approval, the petitioners filed a motion for dismissal of the petition for approval against the CEO's, leaving only the banks. On 3 February 2014, the petitioners filed a petition to amend the petition for approval of a class action so that the amount claimed would be NIS 11.15 billion. The bank has not yet submitted its response to the petition for amendment.

D. On 27 November, 2013, a petition for approval of a class action was filed in the Central District Court against the Bank, claiming that the Bank calculates incorrectly the theoretical value of options traded on the Tel Aviv Stock Exchange. According to the petitioners, the Bank uses the Black & Scholes mathematical model, which is the model relevant for determining the value of the option, but inserts an erroneous element. The erroneous element, according to the petitioners, is the expiry date of the option. They argue that the Bank adds an extra value date to this element, which affects the theoretical value of the option, and affects the judgment of customers regarding the feasibility of the transaction and its price. They further contend that other financial institutions do not make this mistake. According to the petitioners, they cannot accurately assess the damages, but estimate it to be tens of millions of shekels.

E. On December 2, 2013, a petition for approval of a class action was filed in the Central District Court, against the Bank, on the subject of early repayment commission. According to the petitioners, the manner of calculating early repayment commission by the Bank, both for small loans and for large loans, is not compatible with Proper Conduct of Banking Business Directives. A financial opinion was attached to the petition, according to which the petitioner's personal damages is determined in the amount of about NIS 90 thousand. The petitioners claim that they are unable to assess the total amount of the claim at this stage.

F. On 9 March 2014, a petition was filed in the Tel Aviv District Court to approve a class action against the Bank without specifying the amount claimed. According to the plaintaiff, the Bank collects money from customers unlawfully in two cases. The first is when the Bank allows customers to exceed the credit limit and debits customer accounts with a fee in the amount of NIS 53 in respect of delivering a warning letter of the deviation from the credit limit. Second, "non-approved" deviations from the credit limit are merged into the excess debit balance in the account resulting in the charging of the the maximum rate of interest.

G. On 17 March 2014, the provisional liquidator of a company in liquidation (the "Company" and "the Special Manager") filed a petition in the Central District Court to issue instructions against the Bank, in which it requested that the Court declare that the Bank will bear the payment to the Company of an aggregate amount of NIS 1,200 million, of which an amount of NIS 635 million to cover all the company's debts to its creditors and an amount of NIS 565 million for repayment of the full value of the assets of the Company in the principal amount standing as at 25 March 2001 in the amount of NIS 165 million, plus interest from that date at the rate it was obliged to pay the Bank. According to the special manager, the Bank is to bear individual responsibility for the liabilities of the company, since allegedly the Bank is to be deemed an "office holder" in the company due to its control over the company, and because the Bank was such, the company's officers were obliged and did act according to its instructions; since the Bank is to be deemed as a "director de-facto" or a "shadow director " in the company; because of its responsibility in jointly committing and / or jointly misleading in fraudulent actions detailed in the petition; and because of the Lenders' Liability doctrine. It should be noted that as part of the motion, the liquidator retained the right to file additional proceedings against the Bank and / or other officers of the company and / or individuals on behalf of the Bank and lawyers advising the Bank.

H. On 18 March 2014, a petition was filed in the Central District Court for approval of a class action against the Bank for an asserted amount of about NIS 155 million. According to the plaintiff, as part of the deducting of tax at source carried out by the Bank in securities transactions executed through it, the Bank's computer systems calculate long capital gains and / or short capital losses unlawfully. The incorrect data are presented to customers in the Leumi Trade system and the simulator existing in the system. The "group" for purpose of the proceedings is defined as: 1. anyone who executed securities trading through Leumi Trade, and for whom, within the deduction of tax at source a long capital gain and / or a short capital loss was calculated. 2. anyone who was presented by the Bank and / or by the Leumi Trade system with incorrect representations about capital gains and / or capital losses reflected in securities owned by him. According to the plaintiff, the aggregate damage caused to members of the first group is about NIS 79 million, and the aggregate damage caused to the members of the second group is about NIS 76.5 million.

3. The following are details of claims and petitions for approval of class actions in material amounts that were filed against subsidiaries of the Bank (hereinafter, “the subsidiaries”). In the opinion of the Management of the Bank, and in reliance on the opinion of the management of each of the subsidiaries, which is based on the opinion of subsidiaries' 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 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 ("the Trust Company"), Aaron Biram, Eran Fuchs, Moti Ma’aravi, Rami Ordan, Excellence Nessuah Underwriting (1993) Ltd. and Expert Financing Ltd. The amount claimed against all the respondents in the class action stands at some NIS 286 million. The complaint makes no clear attribution of a specific claimed amount against any of the respondents. The petition for approval refers to debentures issued by Keshet, backed up by notes issued by Lehman Brothers Bankhaus AG. The petitioner claims that on the collapse of Lehman Brothers, the price of the debenture collapsed and trading was suspended. 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 take various actions to prevent or reduce, according to the petitioner, the damage he alleges was caused to the debenture-holders. The Trust Company has filed its response to the petition for approval of the claim as a class action.

B. On 7 October 2013, Leumi Card was served with a petition to approve a class action and a claim that was filed with Tel Aviv District Court, on the utilizing of a credit facility for refueling and the charging of additional amounts for actual refueling, in advance. The claim was filed against all the fuel companies and all the credit card companies. According to the claim, the fuel companies have an arrangement that is hidden from consumers with the credit card companies, under which credit card companies collect different amounts from consumers ranging from NIS 150 to NIS 600 per refueling, in addition to the refueling cost. The total amount of the claim is defined as "the rate of interest the consumer has to pay for the period his account was charged the extra amount or for the period that he could not make use of his full credit facility for a number of days, and is estimated as 1 shekel for each occurrence…" The amount of the claim was not specified.

E. The Bank is a guarantor for members of some of the provident funds that were managed by Leumi Capital Market Services Ltd. (formerly Leumi Gemel Ltd.), whose operations were sold to Psagot Provident Funds Ltd. ("Prizma"). The guarantee secures the repayment of the original principal amounts that were deposited amounting on 31 December 2013 to NIS 2,744 million in nominal values. The value of the assets of the above funds at 31 December 2013 amounts to NIS 5,771 million. In addition, this guarantee does not apply to deposits in accounts that were opened in the above funds from 22 January 2007.

Against the aforesaid liability, Prizma undertook that, in the event the guarantees or any part of them are realized, it would pay the Bank participation in an amount not exceeding NIS 35 million per calendar year, this amount being linked to the Israeli CPI of 30 October 2006 - and until the payment date. A participation amount that is not utilized in a certain year will not be carried forward to future years.

F. Consolidated companies of the Bank which serve as trust companies, as well as a number of banking subsidiaries, perform trust operations. Such operations include mainly trusteeship over funds, securities and real estate; the handling of donations, gifts and bequests; acting as agent in regard to deposits and loans; handling of share transfers; and management of investment accounts. Some of these companies also act as trustees for debenture holders.

G. Letters of indemnity

1. The Bank has undertaken in advance to grant directors and the other officers of the Bank indemnification in respect of monetary liability which may be imposed on them and in respect of reasonable litigation expenses in connection with the privatization of the Bank.

2. The Bank has undertaken in advance to indemnify Leumi Finance Co. Ltd., a fully controlled subsidiary (hereinafter – "the company"), in order for it to carry out the indemnifications which the company gave its directors and officers, and the lawyers dealing with the issues on behalf of the Company, as well as the corporate secretaries, in respect of monetary liability that may be imposed on them and reasonable litigation expenses in connection with the issue of debentures and other financial products by the Company to the public that the Company publishes from time to time. The indemnification is limited to the amounts of the issues executed by the Company.

3. The Bank has undertaken in advance to indemnify the office holders in the Bank and personal managerial contract holders in the Bank who are not officers of the Bank ("the managerial contract holders") with respect to the duties they fulfill with the Bank and in the subsidiaries and other companies on behalf of the Bank and in respect of a list of events as is the generally accepted practice in the banking system in Israel, including, *inter alia*, the routine banking activity of the Bank, an offer of securities to the public pursuant to a prospectus and reports to the public and to the supervisory authorities. The actual fulfillment of the indemnity commitment is subject to the two following cumulative conditions: (1) the maximum amount in respect of the actual realization of the indemnity to all the officers of the Bank and to the officers of the subsidiaries and the managerial contract holders, in respect of monetary liability which may be imposed on any of them, and in respect of reasonable legal fees, in connection with the above events, will not exceed in aggregate 10% (ten percent) of the shareholders' equity of the Bank as defined in the directives of the Supervisor of Banks, as reflected in the last financial statements of the Bank published immediately prior to the date of the actual indemnification; (2) the maximum amount in respect of the actual realization of the indemnity does not impair the minimum capital requirement in accordance with the directives of the Supervisor of Banks. The obligation for indemnification is also for reasonable litigation expenses incurred as a result of an investigation or proceeding that ended without an indictment being filed and without a financial liability being imposed as an alternative to criminal proceedings, or that ended without an indictment being filed but with a financial liability being imposed as an alternative to criminal proceedings for an infraction that does not require proof of criminal intent, or in connection with a monetary sanction. The letter of indemnity also includes a further obligation for indemnification for expenses and/or payment to the injured party of a breach in accordance with and subject to that stipulated in the Streamlining of Enforcement Proceedings in the Securities Authority Law (Legislative Amendments), 2011 ("the Streamlining of Enforcement Proceedings Law"), as well as expenses in connection with proceedings under Section G-1 of the Antitrust Law, 1988. The obligation for indemnification will be in effect only after exhaustion of the rights of the officer toward a third party (e.g. an insurer).

In addition, the Bank granted exemption from liability to officers in the Bank and personal contract holders for damage as a result of breach of their obligation of caution *vis-à-vis* the Bank.

The Bank also undertook in advance to indemnify the legal advisor to the Board of Directors of the Bank in respect of legal services provided to the Board of Directors, to the Bank and to the Directors as legal advisor to the Board of Directors, in similar wording to the indemnity given to officers. The Bank exempted the legal advisor to the Board of Directors from liability in connection with the provision of the said legal services.

4. The Bank has undertaken to indemnify employees of the Bank for expenses and/or payment to the injured party of a breach or subject to that stipulated in the Streamlining of Enforcement Proceedings Law, in accordance with the usual terms appearing in letters of indemnity given by the Bank.

5. The Bank has undertaken to indemnify external advisors in respect of an obligation or loss including in respect of other legal expenses in connection with the services given by them to the Bank.

6. The Bank has undertaken to indemnify Tamir Fishman Trusteeships 2004 Ltd. (“Tamir Fishman”) in connection with the option plan and the plan to offer shares to employees of the Bank, Leumi Mortgage Bank Ltd., Arab-Israel Bank Ltd. and the Bank Leumi le-Israel Employees Restaurant Association, for any damage and/or expense and/or loss actually borne by Tamir Fishman (including lawyers' fees) following a final judgment verdict against Tamir Fishman in favor of any third party whomsoever, in connection with or as a result of the fulfillment of its duties in accordance with the trust agreements signed pursuant to the above plans, and in accordance with any law.

7. The Bank and subsidiary companies have undertaken to indemnify the international credit companies "Visa" and "MasterCard" in respect of fulfillment of the obligations of the subsidiaries concerning “Visa” and “MasterCard” credit card activity, whichever applicable.

8. Pursuant to the merger agreement between the Bank and Leumi Mortgage Bank Ltd. ("Leumi Mortgage") from 10 September 2012, the Bank assumed, in place of Leumi Mortgage for all intents and purposes, as of 31 December 2012, all the liabilities of Leumi Mortgage, including any commitment of agreement of any type, including letters of indemnity given by Leumi Mortgage to office holders of Leumi Mortgage.

9. From time to time, the Bank provides subsidiary companies with letters of indemnity, limited and unlimited as to amount and period, to secure indemnities granted by them to officer holders due to risks applicable to office holders in the companies, and for purposes of the subsidiary companies complying with regulatory directives. In addition, the Bank has given letters of indemnity to Bank employees and to office holders of subsidiaries in respect of a list of events which are specified therein.

10. The Bank and its subsidiaries, from time to time and in circumstances generally accepted in the normal course of business, are accustomed to give letters of indemnification, limited and unlimited as to amount and period.

H. Credit Cards

1. In 2006, an arrangement was submitted for approval of the Antitrust Tribunal (hereinafter: "the tribunal") that was reached between Leumi Card, IsraCard Ltd., Israel Credit Cards Ltd., and the banks controlling each one of these companies (hereinafter "the parties requesting approval"), with regard to the issuer's commission rates (cross-commission) paid by the credit card clearers (the credit card companies) to their issuers, and the structure of categories in commission rates during the application of the arrangement.

On 7 March 2012, the Antitrust Tribunal gave its judicial approval to an agreement submitted in the above proceedings by the plaintiffs and the Commissioner (hereinafter: "the agreement") in which the parties agreed on the average rate of cross-commission to prevail over the length of the agreement, and the outline reduction of this rate over the years, such that from 1 July 2014 until the end of the period of the agreement, the average rate will equal the issuer's commission of 0.7%. The arrangement is in force until the end of 2018.

On 29 March 2012, an appeal was filed in the Supreme Court by one of the companies opposing the agreement, against the verdict of the Antitrust Tribunal that approved the agreement. The appeal did not relate to the rate of cross-commission, or the rate of reduction as set out in the verdict of the Antitrust tribunal, but to the manner of classifying the appellant company in a certain category of vendors paying a higher cross-commission than the minimum commission in the agreement. In the hearing that took place on 17 March 2014, the Supreme Court rejected the appeal and ordered the appellant to pay the expenses of the respondents.

The said arrangement is expected to materially affect both Leumi Card’s income as an issuer and also its expenses as a clearer in the coming years.

2. The Bank has undertaken with regard to Visa International to take full responsibility for the proper execution by Leumi Card of all the provisions and requirements included in the Articles of Visa International as in effect from time to time, to perform all actions necessary in order to fulfill its commitment and to notify Visa International immediately in writing regarding any material change in the agreement between the Bank and Leumi Card.

3. The Bank has undertaken with regard to World MasterCard and to all other Mastercard members to take full responsibility for carrying out all Leumi Card's obligations under the Articles of World MasterCard and its principles and to indemnify these entities for any loss, cost, expense or debt in respect of an infringement of Leumi Card's aforesaid obligations.

Note 18 - Contingent Liabilities and Special Commitments (cont'd)

I. Israel Corporation Ltd. – a company included on equity basis

1. A company included on equity basis of the Israel Corporation Ltd. had a working capital deficit at September 30, 2013, negative cash flow from current operations for the three months that ended on that date, and other issues related to the business situation of the company. The management of the above company has plans to increase its positive cash flow and improve profitability including an outline plan for agreements in principle obtained after the date of the report, with the financing banks subject to the conditions specified therein. The management of the above company believes that the conditions precedent set forth therein are expected to be met with a high degree of probability.

In addition, there are outstanding legal proceedings, claims have been filed, and there are other contingencies, against the above company.

The management of the above company, based on the opinions of their legal advisors, cannot estimate the amount of the exposure from the said legal proceedings, claims and contingencies, if any, and therefore, no provision has been made in this regard in the financial statements of the Israel Corporation Ltd. and the above company.

2. A consolidated company of the Israel Corporation has a dependency on the obtaining of an overall debt settlement with lenders to finance its liabilities and negative working capital that raises significant doubt regarding its continued existence as a "going concern". The financial statements of the above consolidated company do not include any adjustments that might be necessary if it cannot continue as a "going concern".

3. The Israel Corporation has announced an examination of the split of its holdings, such that the Israel Corporation will continue to hold Israel Chemicals Ltd and Oil Refineries Ltd., while its remaining holdings will be transferred and held by all the shareholders in the Israel Corporation through a new company.
The split plan, in its final format to be determined, may not be able to be exercised, in whole or in part, or may be implemented in a different format than the one being examined in a timeframe other than that expected. The Bank is examining the impact of the split.

4. At the end of July 2013, the Russian potassium producer, Uralkali, announced its withdrawal from the potassium marketing company, jointly owned by it and Belaruskali (BPC), through which the two producers, Uralkali and Belaruskali, will export their product outside of their countries. At the same time as the withdrawal notice, Uralkali also announced a change in its sales strategy and a switch to a policy of favoring quantity over price, taking full advantage of the company's production capacity. This announcement triggered a process of reduction in potassium prices in the markets and led to a deferral in the purchase of potassium by customers in expectation of further price decreases. During the fourth quarter there was renewed demand, the level of activity in the various markets returned to a normal level and prices stabilized.

For further information on these matters, see the financial statements of the Israel Corporation Ltd. at 31 December 2013.

J. On 26 April 2009, a ruling of the Antitrust General Director was received by 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 submitted an appeal against this ruling. On 22 February 2011, the response of the Commissioner to the appeal was submitted. On 29 July 2012, the Bank received the letter of the Antitrust Tribunal according to which the Commissioner is considering publishing a supplementary ruling regarding the transfer of information detailed in the Commissioner's response to the appeal, but were deleted from it at the request of the banks, according to which these transfers of information constituted restrictive practices. The Bank was given the opportunity to submit its position to the Commissioner before the Commissioner makes his decision to publish the above-mentioned supplementary ruling. Following negotiations that took place between the banks and the Commissioner, agreement in principle was formulated between the parties for a compromise according to which the Antitrust Tribunal would be requested to approve an agreed order bringing to an end the proceedings deriving from the investigation that led to the publishing of the decision. According to the wording of the agreed order formulated by the parties, the decision would be canceled but the Bank will pay the Treasury an amount of about NIS 21 million (and additional amounts will be paid by other banks) when the Bank will have the possibility of paying the said amount (and the other banks with regard to the amounts relevant to them), instead of a payment to the Treasury and subject to conditions stipulated in the wording of the agreed order, in the framework of compromise arrangements in a number of petitions for approval of class actions outstanding against the Bank.

K. As mentioned in the previous financial statements, the United States authorities (the “U.S. authorities”) are conducting extensive investigations of foreign banks in connection with their activity with customers who are U.S. taxpayers ("the U.S. customers"), on suspicion of a breach of U.S. law. As part of these investigations that are taking place also against the Group, the U.S. authorities issued various subpoenas for receipt of information and documents concerning banking services given to the U.S. customers by the Group.

The Bank made a provision to cover the anticipated expenses in this connection, including those of advisors, service providers and outside experts. The balance of the provision at 31 December 2014 amounts to about NIS 490 million.

With regards to the total amount of expenses incurred in respect of the U.S. customers, see Note 25 – Other Operating Expenses.

This provision does not constitute any acknowledgement to any claim that may be raised against the Group by the U.S. Authorities.

Investigations by the U.S. authorities are continuing and ongoing contacts are taking place between the Group and the authorities aimed at reaching a solution in the matter. The Group is cooperating with the U.S. authorities, subject to that allowed under the law.

In light of the fact that there is still no certainty regarding the amount of expense that may be caused to the Group in this connection, it is possible that the final expense amount will be significantly higher than the amount included in the financial statements.

L. On 26 August 2013, the Antitrust Commissioner ("the Commissioner") granted the exemption regarding the joint holdings of Bank Leumi, Bank Hapoalim, Discount Bank, First International Bank and Bank Mizrahi-Tefahot (hereinafter, together – "the Banks") in Automatic Bank Services Ltd. (hereinafter "ABS"), for a period of three years. Pursuant to the exemption, further terms were stipulated in addition to those provided in previous exemptions granted by the Commissioner, including some concerning the resilience of the technological interface for providing gathering and approval services and interface services that will be developed and assimilated in ABS systems under various conditions determined by the Commissioner in the exemption, the principal of which is the provision of a possibility for rapid connection under equitable conditions and at a low cost of various entities that are entitled under the law to connect to ABS, with effect from 1 October 2015. On 7 August 2013 and 30 January 2014, ABS signed an agreement to sell its automated cash-dispensing activity, subject to fulfillment of the conditions precedent in the agreement, pursuant to the decision of the Commissioner on this matter. The approval of the Commissioner to the amendment of the agreement has not yet been received.

Note 18 - Contingent Liabilities and Special Commitments (cont'd)

M. In March 2012, an indictment was served against Leumi Romania and against members of the credit committee of Leumi Romania, regarding a transaction in the account of a customer, who, according to the General Prosecutor in Romania, was carried out unlawfully. The indictment was submitted as a result of a complaint by the customer who alleged that he incurred damage as the result of the Bank's action (the amount of the damage is not material). On 28 November 2012, the court in Romania accepted Bank Leumi Romania's arguments that the General Prosecutor in Romania had no authority to serve an indictment against it and certain employees/managers, and decided to send the case back to the General Prosecutor for rewording and resubmission of the indictment. The General Prosecutor and the complainant appealed the decision. The appeal was approved, the case was sent back to the lower court and a date was set for the hearing.

N. On September 1, 2013, a petition for approval of a derivative action was filed in the Economic Department of the Tel Aviv District Court against former senior officers of the Bank. The petitioner claimed that, as part of investigations of the U.S. tax authorities, it was found that representatives of the Bank and representatives of Bank Leumi USA assisted customers that are U.S. taxpayers to execute transactions that prevented the U.S. tax authorities from collecting taxes from their citizens. The damage caused to the Bank, as claimed by the petitioner, amounts to hundreds of millions of shekels that the Bank plans to pay to the U.S. authorities. The plaintiff argued that, as at the stage the petition was filed, the Bank mentioned a sum of NIS 340 million, with part of the amount paid to consultants and service providers in connection with the investigations. The petitioner claims that the former officers are responsible for the damage caused to the Bank by encouraging it to take part in the illegal activity or at least by doing nothing to prevent it.

Note 18A – Derivative Instruments and Hedging Activities on consolidated basis

The Group's activity in derivative instruments

General

The above activity involves taking risks, mainly those discussed below:

- Credit risk measures the maximum loss which will be incurred if the other party fails to discharge its obligations under the transaction. To cover this risk, collateral is required from the client commensurate with the risk on the transactions. The collateral is included in the total amount of collateral required in respect of the client's obligations. For transactions which include the writing of options or the purchase/sale of contracts that are traded on a stock exchange, the clients are required to deposit at least the liquid collateral required by those stock exchanges.

- Market risks include risks due to changes in interest rates and changes in foreign exchange rates, the CPI and stock exchange prices. The market risks relating to transactions in derivatives are part of the total of the market risk relating to financial instruments. Activity in derivatives is carried out within the limits of exposure to market risks determined by the boards of directors of the Group companies.

- Liquidity risk which results from the uncertainty with respect to the price which the Bank will need to pay to cover the transaction. This risk exists mainly with respect to instruments with a low trading volume or a low trading volume in the underlying asset. This risk is taken into account in determining the collateral to be obtained.

- The said activity does not refer to derivative instruments embedded in other activities.

Note 18B – Derivative Instrument Activity - Scope, Credit Risks and Repayment Dates

(a) Scope of activity on consolidated basis

	31 December 2013					
	Interest rate contracts		Foreign currency contracts	Contracts in respect of shares	Commodities and other contracts	Total
	Shekel – index	Other				
	(NIS millions)					
(1) Nominal amount of derivative instruments						
a) Hedging derivatives (1)						
Forward contracts	-	-	1,426	-	-	1,426
Swaps	-	2,581	-	-	-	2,581
Total	-	2,581	1,426	-	-	4,007
Of which: interest-rate swap contracts in which the banking corporation agreed to pay a fixed rate of interest	-	2,485	-	-	-	2,485
b) ALM derivatives (1)(2)						
Futures contracts	-	8,320	348	35,508	6,640	50,816
Forward contracts	12,072	12,015	126,909	3	181	151,180
Exchange-traded options						
Options written	-	4,779	8,586	14,592	405	28,362
Options purchased	-	4,779	8,762	14,592	405	28,538
Other options						
Options written	-	10,710	26,974	864	239	38,787
Options purchased	-	8,102	26,143	796	252	35,293
Swaps	678	287,880	26,099	12,251	197	327,105
Total	12,750	336,585	223,821	78,606	8,319	660,081
Of which: interest-rate swap contracts in which the banking corporation agreed to pay a fixed rate of interest	-	158,832	-	-	-	158,832
c) Other derivatives (1)						
Total	-	-	-	-	-	-
d) Credit derivatives and foreign exchange spot contracts						
Credit derivatives in which the banking corporation is a guarantor	-	-	-	-	-	-
Credit derivatives in which the banking corporation is a beneficiary	-	-	-	-	-	-
Foreign exchange spot contracts	-	-	6,543	-	-	6,543
Total	-	-	6,543	-	-	6,543
Aggregate Total	12,750	339,166	231,790	78,606	8,319	670,631

(1) Excluding credit derivatives and spot foreign currency exchange contracts.
(2) Derivatives constituting part of the assets and liabilities of the Bank not intended for hedging.

Note 18B – Derivative Instrument Activity - Scope, Credit Risks and Repayment Dates (cont'd)

(a) Scope of activity on consolidated basis (cont'd)

	31 December 2013					
	Interest rate contracts		Foreign	Contracts	Commodities	
	Shekel –		currency	in respect	and other	
	index	Other	contracts	of shares	contracts	Total
	(NIS millions)					
(2) Gross fair value of derivative instruments						
a) Hedging derivatives (1)						
Gross positive fair value	-	36	37	-	-	73
Gross negative fair value	-	130	10	-	-	140
b) ALM derivatives (1)(2)						
Gross positive fair value	118	7,928	3,275	1,557	103	12,981
Gross negative fair value	232	7,545	3,894	1,597	95	13,363
c) Other derivatives (1)						
Gross positive fair value	-	-	-	-	-	-
Gross negative fair value	-	-	-	-	-	-
d) Credit derivatives						
Credit derivatives in which the banking institution is a guarantor						
Gross positive fair value	-	-	-	-	-	-
Gross negative fair value	-	-	-	-	-	-
Credit derivatives in which the banking institution is a beneficiary						
Gross positive fair value	-	-	-	-	-	-
Gross negative fair value	-	-	-	-	-	-
e) Total						
Gross positive fair value	118	7,964	3,312	1,557	103	13,054
Fair value amounts offset in the balance sheet	-	-	-	-	-	-
Book value of assets in respect of derivative instruments	118	7,964	3,312	1,557	103	13,054
Of which: book value of assets in respect of derivative instruments not subject to a master netting arrangement or similar arrangements	20	33	250	17	5	325
Gross negative fair value (3)	232	7,675	3,904	1,597	95	13,503
Fair value amounts offset in the balance sheet	-	-	-	-	-	-
Book value of liabilities in respect of derivative instruments	232	7,675	3,904	1,597	95	13,503
Of which: book value of liabilities in respect of derivative instruments not subject to a master netting arrangement or similar arrangements	54	35	528	315	4	936

(1) Excluding credit derivatives and spot foreign currency exchange contracts.
(2) Derivatives constituting part of the assets and liabilities of the Bank not intended for hedging.
(3) Of which: gross negative fair value of liabilities in respect of embedded derivative instruments in the amount of NIS 16 million.

Note 18B – Derivative Instrument Activity - Scope, Credit Risks and Repayment Dates (cont'd)

(a) Scope of activity on consolidated basis (cont'd)

	31 December 2012					
	Interest rate contracts		Foreign currency contracts	Contracts in respect of shares	Commodities and other contracts	Total
	Shekel – index	Other				
	(NIS millions)					
(1) Nominal amount of derivative instruments						
a) Hedging derivatives (1)						
Forward contracts	-	-	1,525	-	-	1,525
Swaps	-	2,659	-	-	-	2,659
Total	-	2,659	1,525	-	-	4,184
Of which: interest-rate swap contracts in which the banking corporation agreed to pay a fixed rate of interest	-	2,613	-	-	-	2,613
b) ALM derivatives (1)(2)						
Futures contracts	-	6,740	232	23,393	2,075	32,440
Forward contracts	14,535	21,450	119,241	-	624	155,850
Exchange-traded options						
Options written	-	2,470	7,048	7,038	614	17,170
Options purchased	-	2,470	7,048	7,038	614	17,170
Other options						
Options written	-	17,589	18,802	1,366	503	38,260
Options purchased	-	17,751	19,038	1,475	526	38,790
Swaps	704	224,499	22,405	6,509	427	254,544
Total	15,239	292,969	193,814	46,819	5,383	554,224
Of which: interest-rate swap contracts in which the banking corporation agreed to pay a fixed rate of interest	-	129,033	-	-	-	129,033
c) Other derivatives (1)						
Total	-	-	-	-	-	-
d) Credit derivatives and foreign exchange spot contracts						
Credit derivatives in which the banking corporation is a guarantor	-	-	-	-	-	-
Credit derivatives in which the banking corporation is a beneficiary	-	-	-	-	187	187
Foreign exchange spot contracts	-	-	8,219	-	-	8,219
Total	-	-	8,219	-	187	8,406
Aggregate Total	15,239	295,628	203,558	46,819	5,570	566,814

(1) Excluding credit derivatives and spot foreign currency exchange contracts.
(2) Derivatives constituting part of the assets and liabilities of the Bank not intended for hedging.

Note 18B – Derivative Instrument Activity - Scope, Credit Risks and Repayment Dates (cont'd)

(a) Scope of activity on consolidated basis (cont'd)

	31 December 2012 (4)					
	Interest rate contracts		Foreign currency contracts	Contracts in respect of shares	Commodities and other contracts	Total
	Shekel – index	Other				
	(NIS millions)					
(2) Gross fair value of derivative instruments						
a) Hedging derivatives (1)						
Gross positive fair value	-	1	30	-	-	31
Gross negative fair value	-	225	22	-	-	247
b) ALM derivatives (1)(2)						
Gross positive fair value	133	8,196	2,493	473	110	11,405
Gross negative fair value	297	7,926	3,726	481	105	12,535
c) Other derivatives (1)						
Gross positive fair value	-	-	-	-	-	-
Gross negative fair value	-	-	-	-	-	-
d) Credit derivatives						
Credit derivatives in which the banking institution is a guarantor						
Gross positive fair value	-	-	-	-	-	-
Gross negative fair value	-	-	-	-	-	-
Credit derivatives in which the banking institution is a beneficiary						
Gross positive fair value	-	-	-	-	2	2
Gross negative fair value	-	-	-	-	-	-
e) Total						
Gross positive fair value	133	8,197	2,523	473	112	11,438
Fair value amounts offset in the balance sheet	-	-	-	-	-	-
Book value of assets in respect of derivative instruments	133	8,197	2,523	473	112	11,438
Of which: book value of assets in respect of derivative instruments not subject to a master netting arrangement or similar arrangements	26	95	296	75	19	511
Gross negative fair value (3)	297	8,151	3,748	481	105	12,782
Fair value amounts offset in the balance sheet	-	-	-	-	-	-
Book value of liabilities in respect of derivative instruments	297	8,151	3,748	481	105	12,782
Of which: book value of liabilities in respect of derivative instruments not subject to a master netting arrangement or similar arrangements	226	28	600	54	18	926

(1) Excluding credit derivatives and spot foreign currency exchange contracts.
(2) Derivatives constituting part of the assets and liabilities of the Bank not intended for hedging.
(3) Of which: gross negative fair value of liabilities in respect of embedded derivative instruments in the amount of NIS 20 million.
(4) As of 1 January 2013, the Bank implemented for the first time the directives of the Supervisor of Banks on offsetting assets and liabilities. Comparative figures for the previous year have been reclassified as far as possible to adapt them to the format required under the said directives.

Note 18B – Derivative Instrument Activity - Scope, Credit Risks and Repayment Dates (cont'd)

b. Credit risk in respect of derivative instruments by counterparty to the contract on consolidated basis

	31 December 2013					
	Stock Exchanges	Banks	Dealers/ brokers	Governments and central banks	Others	Total
	(NIS millions)					
Book balance of assets in respect of derivative instruments (2)	**139**	**8,722**	**1,933**	**85**	**2,175**	**13,054**
Gross amounts not offset in the balance sheet:						
Mitigation of credit risk in respect of financial instruments	**-**	**6,652**	**1,755**	**-**	**821**	**9,228**
Mitigation of credit risk in respect of cash collateral received	**-**	**938**	**90**	**32**	**43**	**1,103**
Net amount of assets in respect of derivative instruments	**139**	**1,132**	**88**	**53**	**1,311**	**2,723**
Off-balance sheet credit risk in respect of derivative instruments (4)	**-**	**10,519**	**2,269**	**326**	**11,123**	**24,237**
Mitigation of off-balance sheet credit risk	**-**	**3,290**	**448**	**-**	**2,960**	**6,698**
Net off-balance sheet credit risk in respect of derivative instruments	**-**	**7,229**	**1,821**	**326**	**8,163**	**17,539**
Total credit risk in respect of derivative instruments	**139**	**8,361**	**1,909**	**379**	**9,474**	**20,262**
Book balance of liabilities in respect of derivative instruments (2)(3)	**317**	**7,542**	**1,824**	**-**	**3,820**	**13,503**
Gross amounts not offset in the balance sheet:						
Financial instruments	**-**	**6,652**	**1,755**	**-**	**821**	**9,228**
Cash collateral pledged	**-**	**468**	**2**	**-**	**-**	**470**
Net amount of liabilities in respect of derivative instruments	**317**	**422**	**67**	**-**	**2,999**	**3,805**

	31 December 2012 (1)					
	Stock Exchanges	Banks (5)	Dealers/ brokers (5)	Governments and central banks	Others	Total
	(NIS millions)					
Book balance of assets in respect of derivative instruments (2)	143	7,942	1,417	1	1,935	11,438
Gross amounts not offset in the balance sheet:						
Mitigation of credit risk in respect of financial instruments	-	6,443	1,232	1	500	8,176
Mitigation of credit risk in respect of cash collateral received	-	601	-	-	-	601
Net amount of assets in respect of derivative instruments	143	898	185	-	1,435	2,661
Off-balance sheet credit risk in respect of derivative instruments (4)	-	8,840	1,318	201	8,489	18,848
Mitigation of off-balance sheet credit risk	-	1,867	82	121	1,925	3,995
Net off-balance sheet credit risk in respect of derivative instruments	-	6,973	1,236	80	6,564	14,853
Total credit risk in respect of derivative instruments	143	7,871	1,421	80	7,999	17,514
Book balance of liabilities in respect of derivative instruments (2)(3)	159	8,316	1,690	54	2,563	12,782
Gross amounts not offset in the balance sheet:						
Financial instruments	-	6,981	694	1	500	8,176
Cash collateral pledged	-	885	235	22	-	1,142
Net amount of liabilities in respect of derivative instruments	159	450	761	31	2,063	3,464

Note 18B – Derivative Instrument Activity - Scope, Credit Risks and Repayment Dates (cont'd)

b. Credit risk in respect of derivative instruments by counterparty to the contract on consolidated basis (cont'd)

(1) As of 1 January 2013, the Bank implemented for the first time the directives of the Supervisor of Banks on offsetting assets and liabilities. Comparative figures have been reclassified as far as possible to adapt them to the format required under that stated above.
(2) The Bank did carry out net accounting arrangements.
(3) Of which a book balance of stand-alone derivative instruments in the sum of NIS 13,487 million (31 December 2012 – NIS 12,762 million).
(4) Off-balance sheet credit risk in respect of derivative instruments (including in respect of derivative instruments with negative fair value) as calculated for purposes of limitations on debts of borrowers.
(5) Restated.

Note 18B – Derivative Instrument Activity - Scope, Credit Risks and Repayment Dates (cont'd)

c. Details of Repayment Dates – Nominal Values: Year-end balances on consolidated basis

	31 December 2013				
	Up to three months	From three months to one year	From one to five years	Over five years	Total
	(NIS millions)				
Interest contracts:					
Shekel – index	**2,151**	**5,044**	**3,748**	**1,807**	**12,750**
Other	**36,396**	**62,942**	**145,728**	**94,100**	**339,166**
Foreign currency contracts	**151,743**	**47,581**	**11,385**	**21,081**	**231,790**
Contracts in respect of shares	**69,192**	**8,597**	**817**	**-**	**78,606**
Commodities and other contracts	**2,214**	**6,079**	**26**	**-**	**8,319**
Total	**261,696**	**130,243**	**161,704**	**116,988**	**670,631**

	31 December 2012				
	Up to three months	From three months to one year	From one to five years	Over five years	Total
	(NIS millions)				
Interest contracts:					
Shekel – index	1,516	7,578	4,735	1,410	15,239
Other	28,086	58,122	125,942	83,478	295,628
Foreign currency contracts	121,092	60,489	8,300	13,677	203,558
Contracts in respect of shares	41,092	3,511	2,216	-	46,819
Commodities and other contracts	3,617	1,558	395	-	5,570
Total	195,403	131,258	141,588	98,565	566,814

Note 18C – Balances and fair value assessments of financial instruments on consolidated basis

(1) General

This note includes information regarding the determination of the fair value of financial instruments according to directives of the Supervisor of Banks. Most of the financial instruments of the Bank do not have a market value because they do not have an active trading market. Their fair value is therefore determined on the basis of the present value of future cash flows, discounted at an interest rate that reflects the interest at which the Bank would have effected a similar transaction on the reporting date. The estimated fair value is calculated by means of estimating future cash flows and a subjective determination of the discount rate. Therefore, in respect of most financial instruments, the reported fair value does not necessarily indicate the realizable value of the financial instrument on the reporting date. The estimate of fair value is made on the basis of interest rates in effect on the reporting date and does not take into account interest rate fluctuations. Under different interest rates the fair value calculated may be significantly different. This is true especially in respect of financial instruments with interest at fixed rates or those which are non-interest bearing. Furthermore, the determination of fair value does not take into account commissions that will be received or paid over the course of business. In addition, the difference between the balance sheet value and the fair value may not be realized because in most cases the Bank may hold the financial instrument until maturity. Therefore, it should be noted that the data included in this note do not purport to reflect the value of the Bank as a going concern. Furthermore, because of the wide range of valuation techniques and estimates that can be applied in the calculation of fair value, caution must be exercised when comparing fair values of different banks.

(2) Principal methods and assumptions used in estimating the fair value of financial instruments

Financial assets:

Credit to the public - the fair value of credit to the public is determined on the basis of the present value of future cash flows discounted at an appropriate discount rate. The balance of credit was classified into a number of categories according to the operating segment and the credit rating of the borrowers. Future cash flows (principal and interest) were calculated in respect of each category according to the various linkage bases. These receipts were discounted at an interest rate that reflects the rate of risk and average margin inherent in that category of credit and the term of the credit.

The interest rate is usually determined according to the interest rate used in similar transactions on the reporting date.

The fair value of debit balances in current accounts was valued at book value.
The fair value of impaired debts was calculated using interest rates that reflect the inherent high credit risk. In any case, these interest rates reflect the highest rates of interest used by the Group in transactions on the reporting date in the same segment.

The fair value of current account balances classified as impaired loans was calculated in accordance with an estimate of their average duration and based on maximum interest rates in the Bank.

The future cash flows in respect of impaired debts were calculated after deducting the effect of accounting write-offs and allowances in respect of credit losses.

Note 18C – Balances and fair value assessments of financial instruments on consolidated basis (cont'd)

Deposits with banks and credit to governments - by the discounted future cash flows method, at interest rates at which similar transactions were executed on the reporting date.

Securities – Quoted securities at their market value. Unquoted securities, shares at cost, and debentures according to a model which takes into account the present value of future cash flows discounted at the appropriate discount rate, and which also takes into account the probability of failure and market value.

Financial liabilities:

Deposits of the public - The balance of the deposits is classified according to a number of categories according to operating segments, adjustment basis and the terms of deposit. Future cash flows (principal and interest) were calculated in respect of each category. These payments were discounted at an interest rate that reflects the average interest rate the Group pays on similar deposits in the same category for the period remaining until maturity. The balance sheet amount of current accounts and deposits without a repayment date is considered to be an estimate of their fair value.

Deposits from banks and deposits from governments - The fair value estimated by the discounted future cash flows method, at the rate of interest at which the Group raises similar deposits on the reporting date.

Debentures, bonds and subordinated notes - At their fair value or by the discounted future cash flows method, at the rate of interest at which the Group raises similar deposits or at the rate at which it issues similar bonds on the reporting date.

Other financial assets and liabilities:

Derivative instruments:

Derivative instruments that have an active market were valued at market value and, when there are a number of markets in which the instrument is traded, the value is determined according to the most active market.

Derivative instruments that are not traded on an active market were valued on the basis of models the Bank uses in its current operations as at the reporting date, which take into account the risks inherent in the financial instrument.

Off-balance sheet financial instruments in which the balance reflects a credit risk:

The balance sheet value approximates the fair value, since the terms of transactions in the balance sheet do not differ materially from the terms of similar transactions on the reporting date.

Note 18C – Balances and fair value assessments of financial instruments on consolidated basis (cont'd)

	31 December 2013				
	Book value	Fair value			
		Level 1 (1)	Level 2 (1)	Level 3 (1)	Total
	(NIS millions)				
Financial assets					
Cash and deposits with banks	44,351	32,061	11,492	823	44,376
Securities (2)	63,735	45,164	15,339	3,232	63,735
Securities borrowed or purchased under agreements to resell	1,360	1,360	-	-	1,360
Credit to the public, net	240,874	2,585	67,719	172,110	242,414
Credit to governments	558	-	47	537	584
Assets in respect of derivative instruments	13,054	1,272	9,971	1,811	13,054
Other financial assets	963	148	-	815	963
Total financial assets	364,895 (3)	82,590	104,568	179,328	366,486
Financial liabilities					
Deposits of the public	286,003	2,828	141,591	143,385	287,804
Deposits from banks	4,310	-	3,862	434	4,296
Deposits from governments	397	-	331	83	414
Securities loaned or sold under agreements to repurchase	624	624	-	-	624
Debentures, bonds and subordinated notes	25,441	22,881	387	4,816	28,084
Liabilities in respect of derivative instruments	13,487	1,281	11,827	379	13,487
Other financial liabilities	7,779	148	-	7,590	7,738
Total financial liabilities	338,041 (3)	27,762	157,998	156,687	342,447
Off-balance sheet financial instruments					
Transactions in which the balance reflects a credit risk	289	-	-	289	289

(1) Level 1 - Fair value measurements using prices quoted in an active market.
Level 2 – Fair value measurements using other significant observable inputs.
Level 3 – Fair value measurements using significant unobservable inputs.

(2) For further details of the book value and fair value of securities, see Note on Securities.

(3) Of which assets and liabilities on NIS 113,851 million and NIS 94,856 million, respectively, whose book value is the same as fair value (instruments that are shown in the balance sheet at fair value) or are an approximation of fair value (instruments for an original period of 3 months for which the book value is used as an approximation of fair value). For further information on instruments measured for fair value on a recurring basis and on a non-recurring basis, see Notes 18D and 18F.

Note 18C – Balances and fair value assessments of financial instruments on consolidated basis (cont'd)

	31 December 2012				
	Book value	Fair value			
		Level 1 (1)	Level 2 (1)	Level 3 (1)	Total
	(NIS millions)				
Financial assets					
Cash and deposits with banks	54,621	40,671	12,925	1,017	54,613
Securities (2)	56,408	40,458	13,102	2,848	56,408
Securities borrowed or purchased under agreements to resell (4)	1,435	1,435	-	-	1,435
Credit to the public, net	241,264	2,018	62,894	177,556	242,468
Credit to governments	442	-	30	450	480
Assets in respect of derivative instruments	11,438	523	9,580	1,335	11,438
Other financial assets	1,244	399	-	845	1,244
Total financial assets	366,852 (3)	85,504	98,531	184,051	368,086
Financial liabilities					
Deposits of the public	289,538	1,957	126,146	163,335	291,438
Deposits from banks	4,073	-	3,172	829	4,001
Deposits from governments	451	-	272	211	483
Securities loaned or sold under agreements to repurchase (4)	1,007	951	56	-	1,007
Debentures, bonds and subordinated notes	27,525	22,616	390	7,330	30,336
Liabilities in respect of derivative instruments	12,762	503	11,787	472	12,762
Other financial liabilities	7,451	399	-	7,026	7,425
Total financial liabilities	342,807 (3)	26,426	141,823	179,203	347,452
Off-balance sheet financial instruments					
Transactions in which the balance reflects a credit risk	283	-	-	283	283

(1) Level 1 - Fair value measurements using prices quoted in an active market.
Level 2 – Fair value measurements using other significant observable inputs.
Level 3 – Fair value measurements using significant unobservable inputs.

(2) For further details of the book value and fair value of securities, see Note on Securities.

(3) Of which assets and liabilities on NIS 99,196 million and NIS 86,777 million, respectively, whose book value is the same as fair value (instruments that are shown in the balance sheet at fair value) or are an approximation of fair value (instruments for an original period of 3 months for which the book value is used as an approximation of fair value). For further information on instruments measured for fair value on a recurring basis and on a non-recurring basis, see Notes 18D and 18F.

(4) Reclassified.

Note 18D – Items measured for fair value on consolidated basis

(a) Items measured for fair value on a recurring basis on consolidated basis

	31 December 2013			
	Fair value measurements using:			
	Prices quoted in an active market (Level 1)	Other significant observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total fair value
	(NIS millions)			
Assets				
Securities available for sale:				
Israeli government bonds	29,185	1,551	-	30,736
Foreign government bonds	3,087	749	7	3,843
Bonds of Israeli financial institutions	45	60	-	105
Bonds of financial institutions abroad	371	4,789	120	5,280
Asset-backed (ABS) or mortgage-backed (MBS) bonds	97	5,516	1,733	7,346
Other bonds in Israel	381	331	9	721
Other bonds abroad	821	1,181	-	2,002
Shares and mutual funds available for sale	1,465	-	-	1,465
Total securities available for sale	35,452	14,177	1,869	51,498
Securities held for trading:				
Israeli government bonds	7,104	-	-	7,104
Foreign government bonds	772	256	-	1,028
Bonds of Israeli financial institutions	327	-	-	327
Bonds of financial institutions abroad	-	116	-	116
Asset-backed (ABS) or mortgage-backed (MBS) bonds	-	279	-	279
Other bonds in Israel	409	-	-	409
Other bonds abroad	9	511	-	520
Shares and mutual funds held for trading	1,091	-	-	1,091
Total securities held for trading	9,712	1,162	-	10,874
Assets in respect of derivative instruments:				
Shekel-index contracts	-	32	86	118
Interest contracts	22	7,551	391	7,964
Foreign currency contracts	5	1,834	1,334	3,173
Share contracts	739	510	-	1,249
Commodity and other contracts	59	44	-	103
Activity in the Maof market	447	-	-	447
Total assets in respect of derivative instruments	1,272	9,971	1,811	13,054
Others:				
Credit and deposits in respect of the lending of securities	2,585	-	-	2,585
Securities borrowed or purchased under agreements to resell	1,360	-	-	1,360
Other	148	-	-	148
Total others	4,093	-	-	4,093
Total assets	50,529	25,310	3,680	79,519

Note 18D – Items measured for fair value on consolidated basis (cont'd)

(a) Items measured for fair value on a recurring basis on consolidated basis (cont'd)

	31 December 2013			
	Fair value measurements using:			
	Prices quoted in an active market (Level 1)	Other significant observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total fair value
	(NIS millions)			
Liabilities:				
Liabilities in respect of derivativeinstruments:				
Shekel-index contracts	-	157	75	232
Interest contracts	22	7,653	-	7,675
Foreign currency contracts	14	3,430	304	3,748
Share contracts	739	551	-	1,290
Commodity and other contracts	59	36	-	95
Activity in the Maof market	447	-	-	447
Total liabilities in respect of derivative instruments	1,281	11,827	379	13,487
Others:				
Deposits in respect of the lending of securities	2,828	17	-	2,845
Securities loaned or sold under agreements to repurchase	624	-	-	624
Other	148	-	-	148
Total others	3,600	17	-	3,617
Total liabilities	4,881	11,844	379	17,104

Note 18D – Items measured for fair value on consolidated basis (cont'd)

(a) Items measured for fair value on a recurring basis on consolidated basis (cont'd)

	31 December 2012			
	Fair value measurements using:			
	Prices quoted in an active market (Level 1)	Other significant observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total fair value
	(NIS millions)			
Assets				
Securities available for sale:				
Israeli government bonds	20,965	2,033	-	22,998
Foreign government bonds	6,261	182	11	6,454
Bonds of Israeli financial institutions	260	63	-	323
Bonds of financial institutions abroad	610	4,548	123	5,281
Asset-backed (ABS) or mortgage-backed (MBS) bonds	113	3,535	1,401	5,049
Other bonds in Israel	645	394	-	1,039
Other bonds abroad	564	945	74	1,583
Shares and mutual funds available for sale	972	-	-	972
Total securities available for sale	30,390	11,700	1,609	43,699
Securities held for trading:				
Israeli government bonds	8,844	136	-	8,980
Foreign government bonds	190	121	-	311
Bonds of Israeli financial institutions	129	-	-	129
Bonds of financial institutions abroad	-	88	-	88
Asset-backed (ABS) or mortgage-backed (MBS) bonds	-	330	-	330
Other bonds in Israel	707	-	-	707
Other bonds abroad	15	727	-	742
Shares and mutual funds held for trading	183	-	-	183
Total securities held for trading	10,068	1,402	-	11,470
Assets in respect of derivative instruments:				
Shekel-index contracts	-	16	117	133
Interest contracts	27	7,597	573	8,197
Foreign currency contracts	31	1,795	619	2,445
Share contracts	210	131	14	355
Commodity and other contracts	59	41	12	112
Activity in the Maof market	196	-	-	196
Total assets in respect of derivative instruments	523	9,580	1,335	11,438
Others:				
Credit and deposits in respect of the lending of securities	2,244	4	-	2,248
Securities borrowed or purchased under agreements to resell (1)	1,435	-	-	1,435
Other	399	-	-	399
Total others	4,078	4	-	4,082
Total assets	45,059	22,686	2,944	70,689

See notes on next page.

Note 18D – Items measured for fair value on consolidated basis (cont'd)

(a) Items measured for fair value on a recurring basis on consolidated basis (cont'd)

	31 December 2012			
	Fair value measurements using:			
	Prices quoted in an active market (Level 1)	Other significant observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total fair value
	(NIS millions)			
Liabilities:				
Liabilities in respect of derivativeinstruments:				
Shekel-index contracts	-	143	154	297
Interest contracts	27	8,124	-	8,151
Foreign currency contracts	10	3,322	318	3,650
Share contracts	209	153	-	362
Commodity and other contracts	60	45	-	105
Activity in the Maof market	197	-	-	197
Total liabilities in respect of derivative instruments	503	11,787	472	12,762
Others:				
Deposits in respect of the lending of securities (1)	1,957	163	-	2,120
Securities loaned or sold under agreements to repurchase (1)	951	56	-	1,007
Other (1)	399	-	-	399
Total others	3,307	219	-	3,526
Total liabilities	3,810	12,006	472	16,288

(1) Reclassified.

Note 18D – Items measured for fair value on consolidated basis (cont'd)

(b) Items measured for fair value on a non-recurring basis on consolidated basis

	31 December 2013				
	Fair value measurements using:				
	Prices quoted in an active market (Level 1)	Other significant observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total fair value	Total profit (loss) from changes in value for period ended 31 December 2013
	(NIS millions)				
Collateral-dependent impaired credit	-	-	2,119	2,119	(236)
Other assets	-	-	-	-	-
Total	-	-	2,119	2,119	(236)

	31 December 2012				
	Fair value measurements using:				
	Prices quoted in an active market (Level 1)	Other significant observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total fair value	Total profit (loss) from changes in value for period ended 31 December 2012
	(NIS millions)				
Collateral-dependent impaired credit	-	-	2,012	2,012	(549)
Other assets	-	-	-	-	-
Total	-	-	2,012	2,012	(549)

Note 18E – Changes in items measured for fair value on a recurring basis included in Level 3 on consolidated basis

	For the year ended 31 December 2013										
		Total realized and unrealized profits (losses)									
	Fair value at beginning of the year	In profit and loss	In other comprehensive profit	Acquisitions and issues	Sales	Extinguish-ments	Adjustments from translation of financial statements	Transfers to Level 3	Transfers from Level 3	Fair value at 31 December 2013	Unrealized profits (losses) in respect of instruments held at 31 December 2013
	(NIS millions)										
Assets											
Securities available for sale:											
Israeli government bonds	-	-	-	-	-	-	-	-	-	-	-
Foreign government bonds	11	(1)	-	-	(4)	-	1	-	-	7	-
Bonds of financial institutions in Israel	-	-	-	-	-	-	-	-	-	-	-
Bonds of financial institutions abroad	123	(2)	-	-	-	(1)	-	-	-	120	-
Asset-backed (ABS) or mortgage-backed (MBS) bonds	1,401	(97)	(15)	1,006	(445)	(118)	1	-	-	1,733	8
Others in Israel	-	(8)	-	-	-	(2)	-	19	-	9	-
Others abroad	74	(1)	-	-	-	(73)	-	-	-	-	-
Total bonds available for sale	1,609	(109)	(15)	1,006	(449)	(194)	2	19	-	1,869	8
Total shares available for sale	-	-	-	-	-	-	-	-	-	-	-
Bonds for trading	-	-	-	-	-	-	-	-	-	-	-
Shares for trading	-	-	-	-	-	-	-	-	-	-	-
Assets in respect of derivative instruments:											
Shekel-index contracts	117	(55)	-	-	-	-	-	38	(14)	86	37
Interest contracts	573	(99)	-	-	-	(83)	-	-	-	391	(364)
Foreign currency contracts	619	(482)	-	1,197	-	-	-	-	-	1,334	(98)
Share contracts	14	(14)	-	-	-	-	-	-	-	-	-
Commodity and other contracts	12	(12)	-	-	-	-	-	-	-	-	-
Activity in the Maof market	-	-	-	-	-	-	-	-	-	-	-
Total assets in respect of derivative instruments	1,335	(662)	-	1,197	-	(83)	-	38	(14)	1,811	(425)
Total others	-	-	-	-	-	-	-	-	-	-	-
Total assets	2,944	(771)	(15)	2,203	(449)	(277)	2	57	(14)	3,680	(417)
Liabilities											
Liabilities in respect of derivative instruments:											
Shekel-index contracts	154	(76)	-	-	-	-	-	19	(22)	75	(66)
Interest contracts	-	-	-	-	-	-	-	-	-	-	-
Foreign currency contracts	318	(14)	-	-	-	-	-	-	-	304	13
Share contracts	-	-	-	-	-	-	-	-	-	-	-
Commodity and other contracts	-	-	-	-	-	-	-	-	-	-	-
Activity in the Maof market	-	-	-	-	-	-	-	-	-	-	-
Total liabilities in respect of derivative instruments	472	(90)	-	-	-	-	-	19	(22)	379	(53)
Total others	-	-	-	-	-	-	-	-	-	-	-
Total liabilities	472	(90)	-	-	-	-	-	19	(22)	379	(53)

Note 18E – Changes in items measured for fair value on a recurring basis included in Level 3 on consolidated basis (cont'd)

	For the year ended 31 December 2012	Total realized and unrealized profits (losses)									
	Fair value at beginning of the year	In profit and loss	In other comprehensive profit	Acquisitions and issues	Sales	Extinguish-ments	Adjustments from translation of financial statements	Transfers to Level 3 (1)	Transfers from Level 3 (1)	Fair value at 31 December 2012	Unrealized profits (losses) in respect of instruments held at 31 December 2012
	(NIS millions)										
Assets											
Securities available for sale:											
Foreign government bonds	10	-	-	1	-	-	-	-	-	11	-
Bonds of financial institutions in Israel	-	-	-	-	-	-	-	-	-	-	-
Bonds of financial institutions abroad	113	2	10	-	-	(2)	-	-	-	123	10
Asset-backed (ABS) or mortgage-backed (MBS) bonds	737	80	96	873	(296)	(90)	1	-	-	1,401	160
Others in Israel	-	-	-	-	-	-	-	-	-	-	-
Others abroad	72	1	2	-	-	(1)	-	-	-	74	3
Total bonds available for sale	932	83	108	874	(296)	(93)	1	-	-	1,609	173
Total shares available for sale	-	-	-	-	-	-	-	-	-	-	-
Bonds for trading	-	-	-	-	-	-	-	-	-	-	-
Shares for trading	-	-	-	-	-	-	-	-	-	-	-
Assets in respect of derivative instruments:											
Shekel-index contracts (1)	84	(3)	-	-	-	-	-	40	(4)	117	104
Interest contracts (1)	1,675	(1,044)	-	-	-	(58)	-	-	-	573	(488)
Foreign currency contracts	1,790	(1,347)	-	176	-	-	-	-	-	619	407
Share contracts	14	-	-	-	-	-	-	-	-	14	14
Commodity and other contracts	2	10	-	-	-	-	-	-	-	12	12
Activity in the Maof market	-	-	-	-	-	-	-	-	-	-	-
instruments	3,565	(2,384)	-	176	-	(58)	-	40	(4)	1,335	49
Total others	-	-	-	-	-	-	-	-	-	-	-
Total assets	4,497	(2,301)	108	1,050	(296)	(151)	1	40	(4)	2,944	222
Liabilities											
Liabilities in respect of derivative instruments:											
Shekel-index contracts (1)	298	(168)	-	-	-	-	-	24	-	154	(91)
Interest contracts (1)	-	-	-	-	-	-	-	-	-	-	-
Foreign currency contracts	361	(43)	-	-	-	-	-	-	-	318	(43)
Share contracts	-	-	-	-	-	-	-	-	-	-	-
Commodity and other contracts	-	-	-	-	-	-	-	-	-	-	-
Activity in the Maof market	-	-	-	-	-	-	-	-	-	-	-
Total liabilities in respect of derivative instruments	659	(211)	-	-	-	-	-	24	-	472	(134)
Total others	-	-	-	-	-	-	-	-	-	-	-
Total liabilities	659	(211)	-	-	-	-	-	24	-	472	(134)

(1) Reclassified.

Note 18F – Quantitative information on items measured for fair value included in Level 3 on consolidated basis

As at 31 December 2013

A. Quantitative information regarding fair value measurement in Level 3 (in NIS million)

	Fair value	Assessment technique	Unobservable inputs	Range	Average (3)
A. Items measured for fair value on a recurring basis					
Assets					
Securities available for sale (1)					
Asset-backed securities (ABS) or Mortgage-backed securities (MBS)	1,733	Discounting cash flows	Margin Probability of default Rate of early repayment Loss rate	75-240 bp 2.5%-6% 10%-20% 30%-40%	167 bp 4.25% 15% 35%
Assets in respect of derivative instruments (2)					
Interest contracts	86	Discounting cash flows	Inflation forecasts	0.19%-1.66%	0.90%
Interest contracts	391	Discounting cash flows	Transaction counterparty risk	0.03%-100% (*)	1.34%
Foreign currency contracts	247	Discounting cash flows	Inflation forecasts	0.19%-1.66%	0.90%
Foreign currency contracts	1,087	Discounting cash flows	Transaction counterparty risk	0.03%-100% (*)	1.34%
Liabilities					
Liabilities in respect of derivative instruments (2)					
Interest contracts	75	Discounting cash flows	Inflation forecasts	0.19%-1.66%	0.90%
Foreign currency contracts	304	Discounting cash flows	Inflation forecasts	0.19%-1.66%	0.90%
B. Items measured for fair value on a non-recurring basis					
Collateral-contingent impaired debt	2,119	Fair value of collateral			

* In respect of a failed counterparty.

B. Qualitative information regarding fair value measurement in Level 3

1. Unobservable inputs used for the fair value measurement of asset-backed or mortgage-backed securities are margin rates, probability of default, early repayment rate, and the severity of a loss in the event of default.
   Any significant increase/decrease in unobservable parameters will be reflected in a significantly lower/higher fair value.
2. Unobservable inputs used for the fair value measurement of derivatives are the credit risk of the counterparty to the transaction and the forecast rate of inflation. The higher/lower the credit risk of the counterparty to the transaction, the lower/higher will be the fair value of the transaction.
   Any change in the forecast rate of inflation will affect the fair value of transactions in accordance with the indexation position of the Bank for these transactions. The more the inflation forecast increases (decreases), and the Bank is committed to pay the amount linked to the index, the fair value of the transactions will decrease (increase). The more the inflation forecast increases (decreases), and the counterparty to the transaction is committed to pay the Bank the amount linked to the index, the fair value of the transactions will increase (decrease).
3. The average figure referring to the unobservable parameter of "Transaction counterparty risk" reflects a weighted average.

Note 18G – Quantitative information on items measured for fair value included in Level 3 on consolidated basis (cont'd)

As at 31 December 2012

A. Quantitative information regarding fair value measurement in Level 3 (in NIS million)

	Fair value	Assessment technique	Unobservable inputs	Range	Average (3)
A. Items measured for fair value on a recurring basis					
Assets					
Securities available for sale (1)					
Asset-backed securities (ABS) or Mortgage-backed securities (MBS)	1,401	Discounting cash flows	Margin Probability of default Rate of early repayment Loss rate	95-778 bp 2%-6% 20% 40%-80%	229 bp 4.50% 20% 60%
Assets in respect of derivative instruments (2)					
Interest contracts	117	Discounting cash flows	Inflation forecasts	0%-1.8%	0.9%
Interest contracts	573	Discounting cash flows	Transaction counterparty risk	0.22%-6.99%	3.61%
Foreign currency contracts	139	Discounting cash flows	Inflation forecasts	0%-1.8%	0.9%
Foreign currency contracts	480	Discounting cash flows	Transaction counterparty risk	0.22%-6.99%	3.61%
Share contracts	14	Discounting cash flows	Transaction counterparty risk	0.22%-6.99%	3.61%
Commodities and other contracts	12	Discounting cash flows	Transaction counterparty risk	0.22%-6.99%	3.61%
Liabilities					
Liabilities in respect of derivative instruments (2)					
Interest contracts	154	Discounting cash flows	Inflation forecasts	0%-1.8%	0.9%
Foreign currency contracts	318	Discounting cash flows	Inflation forecasts	0%-1.8%	0.9%
B. Items measured for fair value on a non-recurring basis					
Collateral-contingent impaired debt	2,102	Fair value of collateral			

* In respect of a failed counterparty.

B. Qualitative information regarding fair value measurement in Level 3

1. Unobservable inputs used for the fair value measurement of asset-backed or mortgage-backed securities are margin rates, probability of default, early repayment rate, and the severity of a loss in the event of default. Any significant increase/decrease in unobservable parameters will be reflected in a significantly lower/higher fair value.

2. Unobservable inputs used for the fair value measurement of derivatives are the credit risk of the counterparty to the transaction and the forecast rate of inflation. Any change in the forecast rate of inflation will affect the fair value of transactions in accordance with the indexation position of the Bank for these transactions. The more the inflation forecast increases (decreases), and the Bank is committed to pay the amount linked to the index, the fair value of the transactions will decrease (increase). The more the inflation forecast increases (decreases), and the counterparty to the transaction is committed to pay the Bank the amount linked to the index, the fair value of the transactions will increase (decrease).

Note 19 - Interested Parties and Related Parties of the Bank and its Consolidated Companies

Control of the Bank

Bank without a controlling core

As of 24 March 2012, the Bank is defined, pursuant to the provisions of the law, as a banking corporation without a controlling core and with no shareholder specified as the controlling shareholder in the Bank.

For current information on the holdings of interested parties in the Bank, see Immediate Report on the Status of Holdings of Interested Parties and Senior Office Holders dated 6 March 2014 (Reference: 2014-01-007785).

Note 19 - Interested Parties and Related Parties of the Bank and its Consolidated Companies (cont'd)

A. Balance sheet and off-balance sheet balances

	31 December 2013												
	Interested parties (6)							Related parties held by the Bank					
	Controlling owners		Key management personnel (1)		Others (2)		Interested party at time of transaction	Unconsolidated subsidiaries		Companies included on equity basis		Others (3)	
	Balance as at 31 December	Highest balance (4)	Balance as at 31 December	Highest balance (4)	Balance as at 31 December	Highest balance (4)	Highest balance (4)	Balance as at 31 December	Highest balance (4)	Balance as at 31 December	Highest balance (4)	Balance as at 31 December	Highest balance (4)
	(NIS millions)												
Assets:													
Deposits in banks	-	-	-	-	-	-	7	-	-	-	-	-	-
Securities (5)	-	-	-	-	-	-	293	-	-	-	-	-	-
Credit to the public, net	173	173	37	37	941	941	2,137	-	-	253	331	1,648	2,103
Investments in companies included on equity basis (5)	-	-	-	-	-	-	-	-	-	1,689	2,122	-	-
Other assets	-	-	-	-	129	129	176	-	-	5	19	10	42
Liabilities:													
Deposits of the public	29	36	29	41	8,544	8,544	6,240	6	17	859	1,322	369	531
Deposits from banks	-	-	-	-	-	-	190	-	-	24	38	-	-
Debentures, bonds and subordinated notes	-	-	2	2	3,232	3,232	684	2	3	-	-	-	-
Other liabilities	-	-	3	3	180	180	383	-	-	104	120	63	84
Credit risk in off-balance sheet items (7)	-	10	18	18	1,856	1,856	1,695	-	-	37	73	996	996

(1) Including their close relatives as defined in IAS 24.
(2) Corporations in which a person or a corporation included in one of the groups on the interested parties, controls them or has joint control in them, has significant influence or holds 25% or more of the issued share capital or the voting rights or is entitled to appoint 25% or more of their directors.
(3) Parties meeting the definition of a related party according to IAS 24 that were not included in other columns, and a party on whose business the activity of the Bank and its consolidated companies is significantly dependent.
(4) Based on end of month balances.
(5) For details, see Note 3 - Securities and Note 6 - Investments in Companies Included on Equity Basis.
(6) At 31 December 2013, holdings of interested parties and related parties in the equity of the Bank were NIS 177,108,758 nominal value of shares in the Bank.
(7) Credit risk in off-balance sheet financial instruments as calculated for purposes of single borrower debt limitations.

Note 19 - Interested Parties and Related Parties of the Bank and its Consolidated Companies (cont'd)
A. Balance sheet and off-balance sheet balances (cont'd)

	31 December 2012												
	Interested parties (6)							Related parties held by the Bank					
	Controlling owners		Key management personnel (1)		Others (2)		Interested party at time of transaction	Unconsolidated subsidiaries		Companies included on equity basis		Others (3)	
	Balance as at 31 December	Highest balance (4)	Balance as at 31 December	Highest balance (4)	Balance as at 31 December	Highest balance (4)	Highest balance (4)	Balance as at 31 December	Highest balance (4)	Balance as at 31 December	Highest balance (4)	Balance as at 31 December	Highest balance (4)
	(NIS millions)												
Assets:													
Deposits in banks	-	-	-	-	-	-	-	-	-	-	-	-	-
Securities (5)	-	-	-	-	594	594	-	-	-	-	-	-	-
Credit to the public, net	2,016	2,016	29	29	-	-	-	-	-	319	369	1,800	2,523
Investments in companies included on equity basis (5) (8)	-	-	-	-	-	-	-	-	-	2,129	2,303	-	-
Other assets	-	4	-	1	19	56	-	-	-	18	40	45	142
Liabilities:													
Deposits of the public	31	718	62	146	1,072	1,072	3	8	8	1,551	1,776	666	1,329
Deposits from banks	-	-	-	-	261	261	-	-	-	37	37	-	-
Debentures, bonds and subordinated notes	-	11	2	2	2,292	2,292	-	-	-	2	2	-	-
Other liabilities	-	15	1	1	227	227	-	-	-	122	122	76	93
Credit risk in off-balance sheet items (7)	-	2,046	18	19	152	283	-	-	-	31	46	676	685

(1) Including their close relatives as defined in IAS 24.
(2) Corporations in which a person or a corporation included in one of the groups on the interested parties, controls them or has joint control in them, has significant influence or holds 25% or more of the issued share capital or the voting rights or is entitled to appoint 25% or more of their directors.
(3) Parties meeting the definition of a related party according to IAS 24 that were not included in other columns, and a party on whose business the activity of the Bank and its consolidated companies is significantly dependent.
(4) Based on end-of-month balances.
(5) For details, see Note 3 - Securities and Note 6 - Investments in Companies Included on Equity Basis.
(6) At 31 December 2012, holdings of interested parties and related parties in the equity of the Bank were NIS 185,510,497 nominal value of shares in the Bank.
(7) Credit risk in off-balance sheet financial instruments as calculated for purposes of single borrower debt limitations.
(8) Restated.

Note 19 - Interested Parties and Related Parties of the Bank and its Consolidated Companies (cont'd)

B. Condensed results of operations with interested and related parties

	2013					
	Interested parties			Related parties held by the banking corporation		
	Shareholders Controlling owners	Key management personnel (1)	Others (2)	Subsidiaries (unconsolidated)	Companies on equity basis or companies held under joint control	Others
	(NIS millions)					
Net interest income (4)	59	1	(321)	(4)	7	87
Non-interest income	-	-	(589)	-	(31)	(8)
Of which: management fees and services	-	-	16	-	-	12
Operating and other expenses (5)	-	(76)	44	-	(19)	-
Total	59	(75)	(866)	(4)	(43)	79

	2012					
	Interested parties			Related parties held by the banking corporation		
	Shareholders Controlling owners	Key management personnel (1)	Others (2)	Subsidiaries (unconsolidated)	Companies on equity basis or companies held under joint control	Others
	(NIS millions)					
Net interest income (4)	15	(1)	(18)	-	2	83
Non-interest income	(27)	-	(184)	-	(25)	69
Of which: management fees and services	3	-	6	-	-	12
Operating and other expenses (5)	-	(72)	62	-	(16)	5
Total	(12)	(73)	(140)	-	(39)	157

	2011					
	Interested parties			Related parties held by the banking corporation		
	Shareholders Controlling owners	Key management personnel (1)	Others (2)	Subsidiaries (unconsolidated)	Companies on equity basis or companies held under joint control	Others
	(NIS millions)					
Net interest income (4)	(5)	-	(11)	-	(13)	101
Expenses in respect of credit losses	-	-	-	-	-	(1)
Non-interest income	-	-	55	-	4	21
Operating and other expenses (5)	-	(60)	(1)	-	(73)	(14)
Total	(5)	(60)	43	-	(82)	107

(1) Including their close relatives as defined in IAS 24.

(2) Corporations in which a person or a corporation included in one of the groups on the interested parties, controls them or has joint control in them, has significant influence or holds 25% or more of the issued share capital or the voting rights or is entitled to appoint 25% or more of their directors.

(3) Parties meeting the definition of a related party according to IAS 24 that were not included in other columns, and a party on whose business the activity of the Bank and its consolidated companies is significantly dependent.

(4) See details in paragraph D below.

(5) See details in paragraph C below.

Note 19 - Interested Parties and Related Parties of the Bank and its Consolidated Companies (cont'd)

C. Remuneration and all other benefits to interested parties

	2013		2012		2011	
	Key management personnel					
	Total benefits	Number of recipients	Total benefits	Number of recipients	Total benefits	Number of recipients
	(NIS millions)		(NIS millions)		(NIS millions)	
Interested parties employed in the banking corporation or on its behalf (1) (2) (3)	**62**	**28**	57	24	45	20
Directors not employed by the banking corporation or on its behalf (1)	**11**	**14**	11	16	12	18

(1) Does not include salary tax expenses.

(2) Of which: short term employee benefits NIS 46 million, post retirement benefits NIS 6 million, other long term benefits NIS 0 million (2012 - short term employee benefits NIS 36 million, post retirement benefits NIS 20 million, other long term benefits NIS 1 million; 2011 - short term employee benefits NIS 31 million, post retirement benefits NIS 9 million, other long term benefits NIS 5 million.).

(3) Of which: share-based payment in the amount of NIS 10 million in 2013.

Directors and officers have been insured by the Bank under a policy for insuring the liability of directors and other officers of the Bank and investee companies. The aggregate insurance premium amounted to NIS 3,351 thousand (2012 - NIS 2,901 thousand, 2011 – NIS 3,001 thousand).

D. Total interest income, net before expenses in respect of credit losses in transactions by the Bank and consolidated companies with interested parties and related parties

	2013		2012		2011 (1)	
	Consolidated	**Of which: companies included on equity basis**	Consolidated	Of which: companies included on equity basis	Consolidated	Of which: companies included on equity basis
	(NIS millions)		(NIS millions)		(NIS millions)	
a) In respect of assets						
From credit to the public	**183**	**13**	123	15	135	7
b) In respect of liabilities						
On deposits of the public	**(204)**	**(6)**	(24)	(12)	(53)	(19)
On deposits from banks	**(11)**	**-**	(1)	(1)	(10)	(1)
On other liabilities	**(139)**	**-**	(17)	-	-	-
Total interest income, net	**(171)**	**7**	81	2	72	(13)

(1) Reclassified pursuant to the first-time implementation of the directives of the Supervisor of Banks on the format of the statement of profit and loss.

Note 20 – Interest income and expenses

	2013	2012	2011 (1)
	(NIS millions)		
A. Interest income (2)			
Credit to the public	**10,678**	11,578	12,137
Credit to governments	**23**	21	21
Deposits with banks	**75**	95	208
Deposits with Bank of Israel and cash	**316**	515	663
Interest income from securities borrowed or purchased under agreements to resell	**20**	45	47
Bonds (3)	**1,022**	1,253	1,207
Total interest income	**12,134**	13,507	14,283
B. Interest expenses (2)			
Deposits of the public	**(3,149)**	(4,441)	(5,185)
Deposits from governments	**(8)**	(14)	(22)
Deposits from banks	**(37)**	(58)	(126)
Debentures, bonds and subordinated notes	**(1,569)**	(1,555)	(1,813)
Interest expense from securities loaned or sold under agreements to repurchase	**(14)**	(31)	(30)
Total interest expenses	**(4,777)**	(6,099)	(7,176)
Total interest income, net	**7,357**	7,408	7,107
C. Details of the net effect of hedging derivative financial instruments on interest income and expenses (4)			
Interest income	**(49)**	(50)	(48)
Interest expenses	**-**	(9)	4
D. Details of interest income on accrual basis from bonds			
Available for sale	**814**	966	967
Held for trading	**208**	287	240
Total included in interest income	**1,022**	1,253	1,207

(1) Including effective component of hedge relationships.
(2) Including interest in respect of mortgage-backed bonds (MBS) in the amount of NIS 125 million (2012 - NIS 68 million, 2011 - NIS 63 million).
(3) Details of effect of hedging derivative instruments in sub-paragraphs A. and B.
(4) Restated.

Note 21 – Non-interest financing income

	2013	2012	2011 (1)
	(NIS millions)		
A. Non-interest financing income from activities not for trading purposes			
A.1 From activities in derivative instruments			
Non-effective part of hedging relationships (2)	**12**	6	-
Net income (expenses) in respect of ALM derivative instruments (3)	**(1,392)**	(690)	1,057
Total from activities in derivative instruments	**(1,380)**	(684)	1,057
A.2 From investment in bonds			
Gains on sale of debentures available for sale	**225**	313	315
Losses on sale of debentures available for sale (7)	**(16)**	(22)	(50)
Total from investment in debentures	**209**	291	265
A.3 Exchange rate differentials, net	**1,580**	597	(1,482)
A.4 Gains (losses) on investment in shares			
Gains from sale of shares available for sale (6)	**616**	81	86
Losses on sale of shares available for sale (4)	**(78)**	(171)	(312)
Gain from sale of shares in companies included on equity basis	**18**	24	-
Dividend from shares available for sale	**27**	54	74
Loss on sale of shares in companies included on equity basis	**(3)**	-	-
Total from investment in shares	**580**	(12)	(152)
A.6 Gains (losses), net in respect of loans sold (5)	**99**	-	-
Total non-interest financing income in respect of activities not for trading purposes	**1,088**	192	(312)
B. Non-interest financing income from activities for trading purposes			
Net income in respect of other derivative instruments	**4**	11	7
Realized and unrealized profits (losses) from fair value adjustment of bonds for trading, net (8)	**(54)**	229	176
Realized and unrealized profits (losses) from fair value adjustment of shares for trading, net (9)	**89**	10	137
Dividend received from shares held for trading	**-**	2	3
Total from investment in shares	**39**	252	323

(1) Excluding effective component of hedging relationships.

(2) Derivative instruments which constitute part of the Bank's assets and liability management system and were not designated for hedging relationships.

(3) Including provisions for impairment of NIS 5 million, (2012 – NIS 160 million, 2011 - NIS 271 million.

(4) Including loans sold of NIS 718 million.

(5) Including profit on sale of Migdal shares of NIS 358 million and profit on sale of Caesarstone shares of NIS 86 million.

(6) Including provisions for impairment of NIS 10 million.

(7) Of which part of the profits (losses) of NIS 26 million (2012 and 2011- NIS 192 million and NIS (36) million, respectively), relating to bonds held for trading still held as of balance sheet date.

(8) Of which part of the profits (losses) of NIS 76 million (2012 and 2011 - NIS 12 million and NIS (1) million, respectively), relating to shares held for trading still held as of balance sheet date.

Note 22 – Commissions

	2013	2012	2011 (1)
	(NIS millions)		
Ledger fees	**833**	868	837
Conversion differences	**289**	298	287
Handling of credit	**332**	358	368
Commissions for distribution of financial products (1)	**207**	185	197
Foreign trade activities	**122**	129	126
Income from transactions in securities and certain derivative instruments	**817**	835	793
Credit cards	**907**	864	856
Management fees and commission on life insurance and home insurance	**42**	42	41
Net income from servicing credit portfolios	**31**	37	41
Management, operations, and custody for institutional entities (2)	**57**	51	53
Commissions on financing transactions	**450**	425	414
Other commissions	**101**	107	103
Total operating commissions	**4,188**	4,199	4,116

(1) Mainly distribution fees of mutual funds.
(2) Mainly operations of provident funds.

Note 23 - Other Income

	2013	2012	2011 (1)
	(NIS millions)		
Profit from the realization of aasets received for settlement of loans	**1**	1	2
Profits from severance pay funds	**129**	95	-
Capital gain from sale of buildings and equipment	**35**	6	2
Capital loss from sale of buildings and equipment	**(4)**	(4)	-
Other, net (2)	**41**	33	44
Total other income	**202**	131	48

Note 24 - Salaries and Related Expenses

	2013	2012	2011 (1)
	(NIS millions)		
Salaries	**3,210**	3,025	2,949
Early retirement (2)	**75**	323	-
Severance pay, provident fund, training fund, pension, vacation and long service bonus	**939**	729	682
Expense (income) deriving from share-based payment transactions	**10**	-	13
National Insurance and VAT on salaries	**755**	655	618
Other related expenses	**208**	217	199
Supplementary provisions for related expenses as a result of changes in salaries in the current year	**(23)**	341	600
Total salaries and related expenses	**5,174**	5,290	5,061
Of which: salaries and related expenses abroad	**525**	642	590

(1) Expenses related to early retirement of employees as part of the plan for structural change in the Bank.

Note 25 - Other Expenses

	2013	2012	2011
	(NIS millions)		
Marketing and advertising	**274**	267	283
Legal, audit and professional consultants	**285**	321	377
Communications - postage, telephone, delivery services, etc.	**171**	171	161
Computers (1)	**240**	240	222
Office expenses	**74**	79	84
Insurance	**26**	21	20
Training	**22**	19	27
Commissions	**164**	162	136
Loss in respect of assets received in settlement of loans	**3**	12	14
Other (2)	**579** (3)	676 (3)	250
Total other expenses	**1,838**	1,968	1,574

(1) The item includes outsourcing expenses and does not include the Bank's computer expenses as the Operations Division is a part of the Bank and its expenses are recorded and classified under the various expense headings.
(2) Regarding directors' fees of the Bank included in this item, see Note 19.D.
(3) Including expenses in respect of US customers, about NIS 236 million (2012 - NIS 400 million) – see Note 18.K.

Note 26 – Provision for taxes on profit

A. Composition of the paragraph

	2013	2012	2011
	(NIS millions)		
Current taxes:			
In respect of current year	**1,419**	1,400	728
In respect of prior years	**99**	46	(2)
Total current taxes	**1,518**	1,446	726
Add (less) changes in deferred taxes			
In respect of current year	**10**	(586)	18
In respect of prior years	**(137)**	(49)	(326)
Total changes in deferred taxes	**(127)**	(635)	(308)
Provision for taxes on income	**1,391**	811	418
Of which: provision for taxes abroad	**61**	74	29
Deferred taxes:			
Creation and reversal of temporary differences	**10**	(586)	18
Change in tax rate	**(137)**	(49)	(326)
Total deferred taxes	**(127)**	(635)	(308)

B. Reconciliation between the theoretical amount of tax applicable if the operating profit were liable for tax at the statutory rate of tax in Israel, and the provision for taxes on the operating profit appearing in the statement of profit and loss:

in Israel, and the adjusted provision for taxes on operating profit appearing in the statemen

	2013	2012	2011
Statutory tax rate applying to a banking corporation	**36.2%**	35.5%	34.5%
	(NIS millions)		
Tax at the statutory tax rate	**1,330**	656	760
Tax (tax saving) resulting from:			
Income of foreign consolidated companies	**29**	2	(106)
Tax exempt and at preferred rates	**(19)**	(17)	(20)
Depreciation differences, depreciation adjustment and capital gain	**25**	4	15
Other non-deductible expenses	**93**	171	103
Timing differences for which deferred taxes have not been recorded	**(42)**	(12)	2
Income of Israeli consolidated companies	**(33)**	(25)	(15)
Change in deferred taxes due to change in tax rates	**(137)**	(49)	(326)
Taxes in respect of prior years	**99**	46	(2)
Other	**46**	35	7
Provision for taxes on profit	**1,391**	811	418

.

Note 26 – Provision for taxes on profit (cont'd)

Changes in tax legislation

On 28 May 2013, the Finance Minister signed an order raising the rate of value added tax in respect of transactions and the import of goods from 17% to 18%, from 2 June 2013.

On 2 June 2013, the Value Added Tax Order (Rate of Tax on Non-Profit Associations and Financial Institutions) (Amendment), 2013 was published, updating the rate of profit tax and salary tax imposed on financial institutions from 17% to 18%. As a result of the said change, the statutory rate of tax applicable to financial institutions increased in 2013 from 35.59% to 36.21%. Furthermore, the rate of salary tax applicable to financial institutions increased from 17% to 18% with respect to the salary payable for work in June 2013 and thereafter.

The change in the rate of profit tax has led to an increase in net balances of deferred tax receivables amounting to NIS 30 million in the third quarter of 2013. The effect of the increase in salary tax on the balance of liabilities to employees as at 30 June 2013 is NIS 53 million before tax and NIS 34 million after tax. The change in salary tax resulted in an increase of NIS 38 million in current salary expenses and operating expenses in the first nine months of 2013, compared to the first nine months of 2012.

On 30 July 2013, the Knesset plenum approved the Economic Plan for 2013-2014 (Law and Budget) which includes, *inter alia*, an increase in the rate of company tax from 25% to 26.5%, with effect from 1 January 2014.

The change in the rate of company tax in the law and the change in profit tax, as set forth below, will raise the statutory tax rate applicable to financial institutions from 36.21% in 2013 to 37.71% in 2014 and thereafter. The change in the rate of company tax led to an increase in the balance of net deferred taxes receivable of some NIS 107 million.

On 13 August 2012, the Deficit Reduction and Change in Tax Burden Law (Legislative Amendment), 2012 (hereinafter: "the Law") was published. Pursuant to the Law, with effect from January 2013, the rate of National Insurance premiums collected from employers in respect of the part of the salary exceeding 60% of the average salary in the market increased from 5.9% to 6.5%. In addition, this rate will increase in January 2014 and January 2015 to 7% and 7.5%, respectively. In addition, on 27 January 2014, the Reliefs and Encouraging of Activity in the Capital Market (Legislative Amendments) Law, 2014 was published, pursuant to which the rate of insurance collected from employers in respect of the part of the salary exceeding 60% of the average salary in the economy will increase in January 2014, January 2015, and January 2016 to 6.75%, 7.25%, and 7.5%, respectively.

Current taxes for the periods reported in these financial statements are calculated in accordance with the tax rates stipulated in the laws mentioned above.

The balances of deferred taxes at 31 December 2013 were calculated at the tax rates as stipulated in the laws mentioned above, in accordance with the rate of tax expected at the date of reversal.

C. On 26 February 2008, the Amendment to the Income Tax (Adjustments for Inflation) Law, 1985 (hereinafter – the Adjustments Law) was passed by the Knesset. The Amendment limits the application of the Law to the years 1985-2007 and determined transition instructions regarding the end of its applicability.

Note 26 – Provision for taxes on profit (cont'd)

D. Amendment 11 to the Income Tax (Inflationary Adjustments) Law states, *inter alia*, that all taxpayers subject to the said Amendment are required to pay tax on profits from securities traded on a stock exchange as at the date of their realization. The Amendment is effective for the years 1999-2007.

In the opinion of the tax authorities and the banks, taxation of securities on the basis of their realization is not appropriate for the activity of financial institutions.

In view of this, on 6 June 1999 the tax authorities submitted to the banks a draft proposed amendment to Article 6 of the said Law, according to which financial institutions will be taxed on the basis of the increase in value of the securities in accordance with the manner of presentation of the securities in the financial statements of the financial institutions.

Notwithstanding the limitation of the application of the Income Tax (Inflationary Adjustments) Law as described above, the Bank, in coordination with the tax authorities, is continuing to act on the basis of the proposed Law and its tax provisions are made accordingly.

E. Final assessments have been issued to the Bank for all years up to and including the tax year 2007. The main consolidated companies have final assessments for the years up to and including 2009.

F. Certain consolidated companies have losses and other deductions which were claimed for tax purposes and in respect of which no future tax saving was included in the balance sheet, amounting in the consolidated companies to some NIS 63 million (31 December 2012 – about NIS 65 million). Utilization of these amounts in the future will be possible if the consolidated companies for which the amounts are recorded have taxable income. Deferred taxes are not recognized in respect of these items since in the opinion of the Group, no taxable income is expected in the future against which tax benefits can be utilized.

Note 26 – Provision for taxes on profit (cont'd)

G. 1. Components of deferred tax assets and the deferred tax reserve are as follows:

	31 December 2013	31 December 2012	31 December 2013	31 December 2012
	(NIS millions)		Average tax rate in percent	
Deferred tax assets				
From allowance for credit losses	**1,077**	1,020	**38%**	37%
From provision for vacation and bonuses	**349**	325	**38%**	36%
From surplus provision for severance pay and pension over funds allocated	**1,607**	1,586	**38%**	36%
From interest not credited to current income	**72**	70	**40%**	39%
From tax deductions carried forward	**55**	70	**36%**	40%
From activity abroad	**7**	3	**38%**	36%
From securities	**30**	-	**42%**	0%
From adjustment of depreciable non-monetary assets	**5**	23	**22%**	17%
Other – from non-monetary assets	**63**	66	**21%**	22%
Total	**3,265**	3,163		
Deferred tax reserve				
From securities	**-**	(135)	**0%**	32%
In respect of investments in investee companies	**(106)**	(191)	**22%**	15%
From adjustment of depreciable non-monetary assets	**(264)**	(279)	**36%**	35%
Other – from monetary assets	**(22)**	(22)	**38%**	36%
Other – from non-monetary assets	**(58)**	(82)	**28%**	27%
Total	**(450)**	(709)		
Deferred taxes receivable, net	**2,815**	2,454		
Deferred taxes included: (1)				
In "Other assets"	**2,955**	2,598		
In "Other liabilities"	**(140)**	(144)		
Deferred tax assets, net	**2,815**	2,454		

(1) The balances of deferred taxes are shown in the consolidated balance sheet in accordance with the classification of the net balance in the books of the Bank and its consolidated companies.

Note 26 – Provision for taxes on profit (cont'd)

G. 2. Movement in deferred tax assets and liabilities relating to the following items:

For the period ended 31 December 2013	Allowance for credit losses	Provision for vacation and bonuses	Surplus of funds over reserve for severance pay and pension	Interest not charged to annual income	Deductions carried forward for tax purposes	Foreign operation	Securities	Investments in investee companies	Adjustment of depreciable non-monetary assets	Other monetary items	Other non-monetary items	Total
	(NIS millions)											
Balance of deferred tax asset (liability) at 1 January 2013	**1,020**	**325**	**1,586**	**70**	**70**	**3**	**(135)**	**(191)**	**(256)**	**(22)**	**(16)**	**2,454**
Changes charged to profit and loss	**9**	**7**	**(55)**	**2**	**(15)**	**21**	**(40)**	**137**	**(3)**	**-**	**21**	**84**
Changes charged to equity	**-**	**-**	**-**	**-**	**-**	**(17)**	**203**	**(46)**	**-**	**-**	**-**	**140**
Effect of the change in the rate of tax	**48**	**17**	**76**	**-**	**-**	**-**	**2**	**(6)**	**-**	**-**	**-**	**137**
Balance of deferred tax asset (liability) at 31 December 2013	**1,077**	**349**	**1,607**	**72**	**55**	**7**	**30**	**(106)**	**(259)**	**(22)**	**5**	**2,815**
Deferred tax asset	**1,077**	**349**	**1,607**	**72**	**55**	**7**	**30**	**-**	**5**	**-**	**63**	**3,265**
Balances available for offsetting												**(310)**
Deferred tax asset at 31 December 2013												**2,955**
Deferred tax liability	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**(106)**	**(264)**	**(22)**	**(58)**	**(450)**
Balances available for offsetting												**(310)**
Deferred tax liability at 31 December 2013												**(140)**

For the period ended 31 December 2012	Allowance for credit losses	Provision for vacation and bonuses	Surplus of funds over reserve for severance pay and pension	Interest not charged to annual income	Deductions carried forward for tax purposes	Foreign operation	Securities	Investments in investee companies	Adjustment of depreciable non-monetary assets	Other monetary items	Other non-monetary items	Total
	(NIS millions)											
Balance of deferred tax asset (liability) at 1 January 2012	916	312	1,371	74	61	-	(91)	(168)	(177)	(26)	6	2,278
Changes charged to profit and loss	82	6	184	(4)	9	9	316	(9)	(7)	4	(22)	568
Changes charged to equity	5	-	-	-	-	(6)	(354)	-	(43)	-	-	(398)
Effect of the change in the rate of tax	17	7	31	-	-	-	(6)	(14)	-	-	-	35
Business combinations	-	-	-	-	-	-	-	-	(29)	-	-	(29)
Balance of deferred tax asset (liability) at 31 December 2012	1,020	325	1,586	70	70	3	(135)	(191)	(256)	(22)	(16)	2,454
Deferred tax asset	1,020	325	1,586	70	70	3	-	-	23	-	66	3,163
Balances available for offsetting												(565)
Deferred tax asset at 31 December 2012												2,598
Deferred tax liability	-	-	-	-	-	-	(135)	(191)	(279)	(22)	(82)	(709)
Balances available for offsetting												(565)
Deferred tax liability at 31 December 2012												(144)

Note 26 – Provision for taxes on profit (cont'd)

G. 3. Taxes on income recognized directly in equity:

	2013			2012			2011		
	Before tax	Tax expense (benefit)	Net of tax	Before tax	Tax expense (benefit)	Net of tax	Before tax	Tax expense (benefit)	Net of tax
	(NIS millions)								
Translation adjustments of financial statements	**-**	**17**	**(17)**	-	6	(6)	-	-	-
Profits (losses) net in respect of net hedges of investments in foreign currency	**203**	**73**	**130**	4	1	3	-	-	-
Financial assets available for sale	**(518)**	**(203)**	**(315)**	1,067	354	713	(1,023)	(336)	(687)
Other comprehensive income in respect of companies included on equity basis	**(85)**	**(27)**	**(58)**	(20)	(2)	(18)	70	7	63
Effect of the Impaired Debts Directive	**-**	**-**	**-**	-	-	-	(1,960)	(584)	(1,376)
Implementation of IAS 12	**-**	**-**	**-**	-	43	(43)	-	-	-
Total recognized in equity	**(400)**	**(140)**	**(260)**	1,051	402	649	(2,913)	(913)	(2,000)

H. Deferred taxes have been calculated at the statutory tax rate applying to the companies at the time of utilization.

I. Under an arrangement with the tax authorities from 14 April 2005, the Bank is entitled as from 2004 to set off, against the tax liability in Israel in respect of income of a subsidiary abroad, a cumulative amount of up to US$ 67 million or the tax liability in Israel, whichever the lower. The amounts not yet set off from the tax liability and in respect of which a future tax saving was not recorded in the balance sheet as of 31 December 2013 is about US$ 54 million. Utilization of these amounts in the future will be possible if the total tax rate applicable to the Bank on its income in Israel is higher than the tax rate to applicable to the foreign subsidiary.

Note 27 – Operating segments and geographic areas

Description of Operating Segments

The Bank in Israel is organized in five business lines, operating through five divisions, each headed by a member of the Management of the Bank. Each business line specializes in providing service to segments of customers (one or more) with similar characteristics and needs. This specialization allows for the provision of a high level of professional service. In addition, there are a number of management units providing various services to the business divisions.

The subsidiary companies in Israel and abroad have been assigned to the relevant business line in accordance with the nature of their activities and the characteristics of their customers.

Principal Operating Segments

Pursuant to Bank of Israel directives, an operating segment is a component which has three characteristics:

1. It engages in business activities from which it is likely to produce income and bear expenses (including income and expenses from transactions with other segments in the Bank).

2. Its operating results are regularly examined by the Management and the Board of Directors in order to make decisions relating to the allocation of resources to the segment and the appraisal of its performance.

3. There is separate financial information with regard to the segment.

The principal operating segments that have been determined under the directives of the Bank of Israel in accordance with the above characteristics are as follows:

1. Households - providing banking services to households and private customers.

2. Small Businesses - providing banking services to small businesses and local authorities.

3. Corporate Banking - providing banking and financial services to major and international companies in the economy for their operations in Israel and abroad.

4. Commercial Banking - providing banking and financial services to middle market companies in the economy and to interested parties in these companies.

5. Private Banking - providing domestic and global financial services and solutions comprehensive to private customers resident in Israel and overseas with large financial asset portfolios.

6. Financial Management and Capital Market - nostro and trading rooms activities and provision of services to institutional customers and foreign financial institutions. Includes the results of activity of investments in (real) companies included on equity basis.

7. Others* - activities not assigned to other segments.

* This includes other activities of the Group, none of which constitutes a profit segment under the directives of the Supervisor of Banks.

Segmented operations also include inter-segmental activity, such as services provided to customers in another segment and also activities (deriving from products) such as mortgage loans, credit cards, capital market, and real estate.

Note 27 – Operating segments and geographic areas (cont'd)

Allocation to a specific operating segment is carried out according to quantitative criteria and additional criteria, such as: size of the approved facility and business turnover, and financial wealth with regard to private customers. Criteria such as the nature of a corporation's business operations and the volume of its business, such as activity volume, international trade volume, complex and special transactions, complex projects and construction financing, can change the segmental allocation of a specific customer.

As mentioned above, the Bank is organized in five business lines, and its policy is to allocate the customers, as much as possible, to the business line/operating segment appropriate for them, in accordance with their characteristics and activities. It should however be emphasized that segmental allocation is determined according to the sector in which the customer's account is actually operated; and until segmentation is carried out between the segments, i.e. until the customer receives service from the segment to which he should be allocated under the above criteria, there is no change to the segmental classification, and the financial results in respect of the customer are recorded in the segment in which his account is actually held.

Financial Measurement System

To provide administrative support for operations according to segments, a profit-center operating and administrative system exists in the Bank according to business lines and additional cross-sections (the "Bachan" system).

The objectives of the system are:

- Measurement of profitability of the different profit centers;
- Measurement of the volume of business activity of the different profit centers according to various classifications;
- Measurement of performance against targets in the work plan;
- Uniformity in analyzing business activity;
- Overall control of business activity and profitability from such activity;
- Directing the business units and the branches to achieving the Bank's targets, including profitability targets;
- To provide a tool for allocating the Bank's resources in a rational manner, on the basis of cost-benefit analysis;
- To provide a basis for appraisal and remuneration.

The basis of the current system ("Bachan System)" in the Bank is the "data warehouse" that centralizes all the Bank's transactions and, with the aid of an appropriate index, enables transactions to be sorted and classified between the different profit centers.

The data presented below regarding operating segments includes the Bank's data in accordance with the principles of the "Bachan" system explained below, while the data for the segments of the subsidiaries in Israel and abroad has been taken from their financial statements, and as defined by them.

In measuring the profitability of overseas subsidiaries, exchange rate differentials, net of tax, arising from financing investments in overseas subsidiaries, are allocated to the net interest income of the overseas units whose functional currency is the same as the functional currency of the Bank.

Note 27 – Operating segments and geographic areas (cont'd)

Income

Net Interest Income

The profit center is credited with interest received from loans that it granted or is debited with interest that is paid on deposits it raised.

At the same time, the profit center granting the loan is debited, and the profit center receiving the deposit is credited, with transfer prices. Transfer prices are usually determined in accordance with market prices with certain adjustments, and generally reflect the risk-free return or marginal costs of raising funds with the same linkage sector and currency and for a similar term. The effects of exchange rate differentials between the shekel/foreign currencies, including adjustments from translating data of overseas units, and also changes in the CPI on surplus uses and/or sources of funds are attributed in the Group to the financial management segment. Under the method described above, the profit centers bear credit risks but do not bear market risks.

The profit and loss account of each of the segments also takes into account the capital allocated to the segment. Each profit center is credited for Tier I capital allocated to it in respect of the risk assets in accordance with risk-free return, and is charged for the additional cost of Tier II capital. Under this method the Bank's available capital is credited with interest equal to the marginal cost of raising funds in accordance with the segment that it is financing, or invested in the capital market. Interest income from management of the nostro is recorded in the financial management and capital markets segment.

Credit Loss Expenses, including the collective allowance, are charged to the profit center in which the customer's account is managed. The same applies to the additional provision required pursuant to the directives of the Bank of Israel.

Non-interest Income

All non-interest income (non-interest financing income, commissions and other income) that the Bank charges its customers and/or its subsidiaries for various services is credited to the profit center in which the customer's account is managed. Income from nostro securities, profits of the severance pay fund and dividends received by the Bank are credited to the financial management and capital market profit center.

Expenses

Expenses are attributed to the lines of business (divisions of the Bank) in accordance with the sectoral association of the customers dealt with by those lines of business.

In a few cases, where the line of business deals with a number of operating segments, the expenses of the lines of business are attributed to the relevant segments and products on the basis of the pricing of multi-dimensional transactions. This pricing is a system in which the transaction cost is calculated taking into account the type of transaction, the type of customer performing it, and the channel in which the transaction was performed.

Pricing is a system in which the cost of transaction is calculated taking into account the type of transaction, the type of customer executing it and the channel in which the transaction was carried out.

Measuring the return on capital

As part of the intensification of measurement of the performance of units and its adjustment to the unique risk characteristics for each unit, measurement is made of the rate of return on risk-adjusted capital (RORAC) of operating segments and their contribution to the Group's profit (Economic Value Added) - EVA, taking into account the cost of capital according to the multi-year return approved by the Board of Directors. The allocation of capital to risk components among the segments was done in accordance with the various risk characteristics inherent in each segment, in accordance with Basel II.

Note 27 – Operating segments and geographic areas (cont'd)

Expenses not related to the direct activity of the profit center (operating segment), such as expenses related to actuarial pension liabilities, are not charged to the profit center but are charged to the financial management segment and others.

The allocation of First Pillar capital (in respect of credit, market and operational risks) is according to Basel II. Credit risks are calculated on the basis of weighted risk assets in the units, and operational and market risks according to the standardized measurement method. Second Pillar Capital is allocated to the units divided into its various components according to models designed by the Bank.

The profit of the operating segments is adjusted for the risk capital in each segment. The risk-adjusted return adjusted was calculated as a ratio of the adjusted profit to the average shareholders' equity allocated to the sector, which constitutes a part of the risk capital allocated (Tier 1 capital, Tier 2 capital and the balance of the capital in respect of extreme scenarios and retained earnings).

For each segment, the profit is calculated, taking into account the cost of Tier 1 and Tier 2 risk capital allocated to each segment. At the Group level, the value added for the shareholders ″EVA″ is the net profit, amended as aforesaid, less the cost of the shareholders' equity, according to the required long-term return over the shareholders' equity, as determined by the Board of Directors.

Note 27 – Operating segments and geographic areas (cont'd)

A. Information on operating segments on consolidated basis for the year ended 31 December 2013

	Households segment	Small Business segment	Corporate segment	Commercial segment	Private Banking segment	Financial Management segment	Other	Total consol-idated
	(NIS millions)							
Interest income, net:								
From outside entities -	2,941	1,125	2,528	1,656	(72)	(821)	-	7,357
Intersegmental -	(293)	(176)	(1,144)	(277)	365	1,513	12	-
Non-interest income:								
From outside entities -	1,640	588	589	492	533	1,531	144	5,517
Intersegmental -	166	(42)	57	83	77	(223)	(118)	-
Total income	4,454	1,495	2,030	1,954	903	2,000	38	12,874
Expenses (income) in respect of credit losses	179	112	(166)	186	9	(52)	-	268
Operating and other expenses	4,094	931	688	1,076	872	1,330	(58)	8,933
Profit before taxes	181	452	1,508	692	22	722	96	3,673
Provision for taxes	49	160	537	277	33	199	136	1,391
Profit (loss) after taxes	132	292	971	415	(11)	523	(40)	2,282
Group equity in after-tax operating profits of companies included on equity basis, net of tax effect	4	-	-	-	-	(297)	-	(293)
Net profit (loss)								
Before attribution to non-controlling interests	136	292	971	415	(11)	226	(40)	1,989
Attributable to non-controlling interests	(27)	(4)	(6)	(3)	(4)	2	-	(42)
Attributable to shareholders of the banking coporation	109	288	965	412	(15)	228	(40)	1,947
Return on capital (percentage profit on relative share of equity of the segment in risk assets)	1.9%	17.2%	11.8%	9.0%	(1.6%)	5.6%	(8.1%)	7.6%

	Households segment	Small Business segment	Corporate segment	Commercial segment	Private Banking segment	Financial Management segment	Other	Total consol-idated
	(NIS millions)							
Average balance of assets	96,033	22,599	66,634	51,342	11,864	113,601	7,765	369,838
Including: investments in companies included on equity basis	2	-	-	-	-	1,971	-	1,973
Average balance of liabilities	124,043	22,704	27,548	51,626	36,884	78,810	2,244	343,859
Average balance of risk assets	68,277	19,898	90,729	53,726	9,285	32,304	6,625	280,844
Average balance of assets of mutual funds and training funds	65,642	3,081	2,366	5,153	8,181	207	-	84,630
Average balance of securities	48,172	6,420	59,121	46,652	76,726	252,582	-	489,673
Average balance of other assets under management	4,357	210	212	653	188	-	2	5,622
Interest income, net:								
Margin on credit-granting activities	1,859	789	1,336	1,087	87	6,257	12	11,427
Margin on deposit-taking activities	789	160	48	292	206	(5,565)	-	(4,070)
Total interest income, net	2,648	949	1,384	1,379	293	692	12	7,357

Note 27 – Operating segments and geographic areas (cont'd)

A. Information on operating segments on consolidated basis (cont'd) for the year ended 31 December 2012[1]

	Households segment	Small Business segment	Corporate segment	Commercial segment	Private Banking segment	Financial Management segment	Other	Total consol-idated
	(NIS millions)							
Interest income, net:								
From outside entities -	1,884	1,097	2,744	1,620	(122)	184	1	7,408
Intersegmental -	915	(173)	(1,196)	(229)	472	198	13	-
Non-interest income:								
From outside entities -	1,622	551	613	517	606	845	20	4,774
Intersegmental -	230	(44)	24	39	51	(245)	(55)	-
Total income	4,651	1,431	2,185	1,947	1,007	982	(21)	12,182
Expenses (income) in respect of credit losses	71	84	933	176	1	(29)	-	1,236
Operating and other expenses	3,872	858	651	1,083	898	1,806	(68)	9,100
Profit (loss) before taxes	708	489	601	688	108	(795)	47	1,846
Provision for (benefit from) taxes	236	167	204	252	31	(251)	172	811
Profit (loss) after taxes	472	322	397	436	77	(544)	(125)	1,035
Group equity in after-tax operating profits of companies included on equity basis, net of tax effect	2	-	-	-	-	(69)	-	(67)
Net profit (loss)								
Before attribution to non-controlling interests	474	322	397	436	77	(613)	(125)	968
Attributable to non-controlling interests	(27)	(3)	(5)	(2)	-	-	-	(37)
Attributable to shareholders of the banking coporation	447	319	392	434	77	(613)	(125)	931
Return on capital (percentage profit on relative share of equity of the segment in risk assets)	9.6%	21.1%	4.3%	10.0%	7.9%	(17.9%)	(29.9%)	3.8%

	Households segment	Small Business segment	Corporate segment	Commercial segment	Private Banking segment	Financial Management segment	Other	Total consol-idated
	(NIS millions)							
Average balance of assets	87,317	20,788	76,624	51,196	13,315	111,951	6,188	367,379
Including: investments in companies included on equity basis	2	-	-	-	-	2,201	-	2,203
Average balance of liabilities	133,814	20,213	30,280	50,486	39,536	65,559	2,874	342,762
Average balance of risk assets	62,105	18,409	104,161	54,607	10,835	30,977	5,876	286,970
Average balance of assets of mutual funds and training funds	53,968	2,175	2,087	3,947	6,668	195	-	69,040
Average balance of securities	49,165	4,753	56,944	42,919	77,003	195,156	-	425,940
Average balance of other assets under management	5,134	226	226	685	227	-	8	6,506
Interest income, net:								
Margin on credit-granting activities	1,726	739	1,484	1,070	97	7,211	14	12,341
Margin on deposit-taking activities	1,073	185	64	321	253	(6,829)	-	(4,933)
Total interest income, net	2,799	924	1,548	1,391	350	382	14	7,408

(1) Reclassified.

Note 27 – Operating segments and geographic areas (cont'd)

A. Information on operating segments on consolidated basis (cont'd) for the year ended 31 December 2011

	Households segment	Small Business segment	Corporate segment	Commercial segment	Private Banking segment	Financial Management segment	Other	Total consol-idated
	(NIS millions)							
Interest income, net:								
From outside entities -	1,614	1,098	2,802	1,595	(81)	79	-	7,107
Intersegmental -	987	(190)	(1,351)	(245)	493	292	14	-
Non-interest income:								
From outside entities -	1,811	548	506	1,046	473	(281)	72	4,175
Intersegmental -	126	(52)	140	(461)	22	330	(105)	-
Total income	4,538	1,404	2,097	1,935	907	420	(19)	11,282
Expenses (income) in respect of credit losses	69	89	312	218	(31)	77	-	734
Operating and other expenses	3,904	829	631	1,047	688	1,317	(75)	8,341
Profit (loss) before taxes	565	486	1,154	670	250	(974)	56	2,207
Provision for (benefit from) taxes	173	168	390	229	75	(421)	(196)	418
Profit (loss) after taxes	392	318	764	441	175	(553)	252	1,789
Companies included on equity basis after the effect of taxes	-	-	-	-	-	148	-	148
Before attribution to non-controlling interests	392	318	764	441	175	(405)	252	1,937
Attributable to non-controlling interests	(28)	(2)	(4)	(1)	(2)	(9)	-	(46)
Attributable to shareholders of the banking coporation	364	316	760	440	173	(414)	252	1,891
Return on capital (percentage profit on relative share of equity of the segment in risk assets)	8.7%	22.7%	9.3%	11.4%	22.0%	(10.1%)	70.1%	8.3%

	Households segment	Small Business segment	Corporate segment	Commercial segment	Private Banking segment	Financial Management segment	Other	Total consol-idated
	(NIS millions)							
Average balance of assets	80,419	19,465	77,596	49,894	11,248	97,642	5,551	341,815
Including: investments in companies included on equity basis	5	-	-	-	-	2,142	-	2,147
Average balance of liabilities	128,256	19,030	35,160	44,043	37,393	53,467	1,197	318,546
Average balance of risk assets	57,268	17,651	99,423	51,073	9,424	38,168	5,444	278,451
Average balance of assets of mutual funds and training funds	53,540	2,199	1,281	4,240	6,390	261	-	67,911
Average balance of securities	50,806	5,702	82,702	40,831	68,071	179,121	-	427,233
Average balance of other assets under management	5,897	244	221	702	224	-	5	7,293
Interest income, net:								
Margin on credit-granting activities	1,443	716	1,387	1,037	107	7,990	16	12,696
Margin on deposit-taking activities	1,158	192	64	313	305	(7,619)	(2)	(5,589)
Total interest income, net	2,601	908	1,451	1,350	412	371	14	7,107

Note 27 – Operating segments and geographic areas (cont'd)

B. Information on activity by geographic area:[1]

31 December 2013

	Israel	USA	UK	Switzerland	Luxembourg	Romania	Others	Total outside of Israel	Total consoli-dated
	(NIS millions)								
Total income (2)	**11,537**	**642**	**217**	**307**	**99**	**49**	**23**	**1,337**	**12,874**
Net profit attributable to shareholders of the banking corporation	**1,993**	**66**	**(66)**	**(57)**	**15**	**(7)**	**3**	**(46)**	**1,947**
Total assets	**338,142**	**18,055**	**9,272**	**5,999**	**1,279**	**1,282**	**331**	**36,218**	**374,360**
Credit to the public, net	**217,381**	**12,926**	**7,155**	**1,917**	**447**	**849**	**199**	**23,493**	**240,874**
Deposits of the public	**256,586**	**13,982**	**7,510**	**5,406**	**1,610**	**707**	**202**	**29,417**	**286,003**

31 December 2012

	Israel	USA	UK	Switzerland	Luxembourg	Romania	Others	Total outside of Israel	Total consoli-dated
	(NIS millions)								
Total income (2)	10,600	702	407	343	24	72	34	1,582	12,182
Net profit attributable to shareholders of the banking corporation	785	90	42	(18)	14	8	10	146	931
Total assets	336,069	20,103	9,732	7,379	989	1,280	608	40,091	376,160
Credit to the public, net	214,668	13,985	7,846	2,998	453	860	454	26,596	241,264
Deposits of the public	256,216	16,336	7,332	6,484	2,010	680	480	33,322	289,538

31 December 2011

	Israel	USA	UK	Switzerland	Luxembourg	Romania	Others	Total outside of Israel	Total consoli-dated
	(NIS millions)								
Total income (2)	10,049	866	490	227	(425)	112	(37)	1,233	11,282
Net profit attributable to shareholders of the banking corporation	1,489	213	102	53	23	(21)	32	402	1,891

(1) The classification was made according to the location of the office.
(2) Interest income net and non-interest income.

Note 28 - Earmarked deposits, credit and deposits from earmarked deposits

	31 December 2013	31 December 2012
	(NIS millions)	
Credit and deposits from earmarked deposits		
Total credit to the public	**111**	158
Earmarked deposits		
Deposits of the public	**2**	6
Deposits from banks	**4**	13
Deposits from the Government	**60**	173
Total	**66**	192

Note 29 – Accumulated Other Comprehensive Income (Loss)

A. Changes in accumulated other comprehensive income (loss), after the effect of tax

	For the year ended 31 December 2013					
	Other comprehensive income before attribution to non-controlling interests					
	Adjustments for presentation of securities available for sale at fair value	Translation adjustments *, net after effect of hedges **	Banking corporation's share in other comprehensive income of investee companies dealt with under the equity method	Total	Other comprehensive income attributed to non-controlling interests	Other comprehensive income attributed to shareholders of the Bank
	(NIS millions)					
Balance at 1 January 2011	468	(474)	39	33	-	33
Net change during the year	(687)	381	73	(233)	(1)	(232)
Balance at 31 December 201	(219)	(93)	112	(200)	(1)	(199)
Net change during the year	713	(56)	-	657	-	657
Balance at 31 December 201	**494**	**(149)**	**112**	**457**	**(1)**	**458**
Net change during the year	**(315)**	**(188)**	**11**	**(492)**	**(3)**	**(489)**
Balance at 31 December 201	**179**	**(337)**	**123**	**(35)**	**(4)**	**(31)**

* Adjustments from translation of financial statements of foreign operations whose functional currency differs from the functional currency of the banking corporation, including adjustments in respect of companies included on equity basis.

** Profit (loss) in respect of hedging net investment in foreign currency.

Note 29 – Accumulated Other Comprehensive Income (Loss) (cont'd)

B. Changes in components of accumulated other comprehensive income (loss), before and after the effect of tax

	2013			2012			2011		
	Before tax	Tax effect	After tax	Before tax	Tax effect	After tax	Before tax	Tax effect	After tax
	(NIS millions)								
Changes in components of other comprehensive income (loss) before attribution to non-controlling interests:									
Adjustments for presentation of securities available for sale at fair value									
Unrealized profits (losses) from adjustments to fair value	**229**	**(79)**	**150**	1,268	(426)	842	(984)	322	(662)
(Profits) losses in respect of securities available for sale reclassified to the statement of profit and loss	**(747)**	**282**	**(465)**	(201)	72	(129)	(39)	14	(25)
Net change in the period	**(518)**	**203**	**(315)**	1,067	(354)	713	(1,023)	336	(687)
Translation adjustments *									
Adjustments for translation of financial statements	**(318)**	**-**	**(318)**	(59)	-	(59)	381	-	381
Hedges **	**203**	**(73)**	**130**	4	(1)	3	-	-	-
Net change in the period	**(115)**	**(73)**	**(188)**	(55)	(1)	(56)	381	-	381
Banking corporation's share in other comprehensive income of investee companies dealt with under the equity base method	**11**	**-**	**11**	-	-	-	73	-	73
Net change in the period	**11**	**-**	**11**	-	-	-	73	-	73
Total net change in the period	**(622)**	**130**	**(492)**	1,012	(355)	657	(569)	336	(233)
Changes in components of other comprehensive income attributed to non-controlling interests:									
Total net change in the period	**(3)**	**-**	**(3)**	1	(1)	-	(2)	1	(1)
Changes in components of other comprehensive income (loss) attributed to shareholders of the banking corporation:									
Total net change in the period	**(619)**	**130**	**(489)**	1,011	(354)	657	(567)	335	(232)

* Adjustments from translation of financial statements of foreign operations whose functional currency differs from the functional currency of the banking corporation, including adjustments in respect of companies included on equity basis. If material, separate disclosure is to be made of the amount of adjustments in respect of companies included on equity basis.

** Profit (loss) in respect of hedging net investment in foreign currency.

Note 30 - Condensed Financial Statements of the Bank

A. Balance Sheet of the Bank as at 31 December 2013

	31 December 201	31 December 2012
	(NIS millions)	
Assets		
Cash and deposits with banks	**40,413**	49,438
Securities	**57,203**	49,475
Securities borrowed or purchased under agreements to repurchase	**1,360**	1,435
Credit to the public	**212,933**	211,255
Allowance for credit losses	**(2,993)**	(3,333)
Credit to the public, net	**209,940**	207,922
Credit to governments	**516**	426
Investments in investee companies	**13,168**	13,513
Buildings and equipment	**3,131**	3,248
Assets in respect of derivative instruments	**12,960**	11,308
Other assets	**4,083**	3,544
Total assets	**342,774**	340,309
Liabilities and equity capital		
Deposits of the public	**273,186**	274,482
Deposits from banks	**7,522**	7,066
Deposits from governments	**155**	260
Securities loaned or sold under agreements to resell	**624**	951
Subordinated notes	**6,526**	6,822
Liabilities in respect of derivative instruments	**13,344**	12,632
Other liabilities	**14,992**	13,175
Total liabilities	**316,349**	315,388
Equity attributable to shareholders of the banking corporation	**26,425**	24,921
Total liabilities and equity	**342,774**	340,309

B. Condensed Statement of Profit and Loss for the year ended 31 December 2013

	2013	2012(1)	2011 (1)
	(NIS millions)		
Interest income	**10,627**	10,859	11,552
Interest expenses	**4,648**	5,521	6,201
Net interest income	**5,979**	5,338	5,351
Expenses in respect of credit losses	**27**	1,069	600
Net interest income after expenses in respect of credit losses	**5,952**	4,269	4,751
Non-interest income			
Non-interest financing income	**928**	386	(221)
Commissions	**2,817**	2,769	2,791
Other income	**165**	110	34
Total non-interest income	**3,910**	3,265	2,604
Operating and other expenses			
Salaries and related expenses	**4,215**	4,104	3,921
Maintenance and depreciation of buildings and equipment	**1,465**	1,400	1,313
Other expenses	**1,233**	1,270	964
Total operating and other expenses	**6,913**	6,774	6,198
Profit before taxes	**2,949**	760	1,157
Provision for taxes on profit	**1,174**	430	198
Profit after taxes	**1,775**	330	959
Bank's share in the profits, net of operating profit of investee companies after the effect of tax	**172**	601	932
Net profit	**1,947**	931	1,891

(1) Figures for 2012 and 2011 do not include Leumi Mortgage which was merged with the Bank in 2013.

C. Statement of Cash Flows
for the year ended 31 December 2013

	2013	2012(1)	2011 (1)
	(NIS millions)		
Cash flows from operating activities			
Net profit for the year	**1,947**	931	1,891
Adjustments:			
Bank's share in undistributed profits of investee companies including extraordinary profits less dividend received	**(51)**	(497)	(482)
Other, net (including provisions for doubtful debts and impairment of securities)	**(806)**	12,796	11,456
Net cash from operating activities	**1,090**	13,230	12,865
Cash flows from activities in assets			
Additional investments in shares of consolidated companies	**-**	(65)	(691)
Proceeds from sale of investments in investee companies	**(5)**	(24,723)	-
Other	**(8,331)**	(5,987)	7,807
Net cash from activities in assets	**(8,336)**	(30,775)	7,116
Cash flows from activities in liabilities and capital			
Dividend paid to shareholders	**(582)**	(2,554)	(149)
Issue of shares to employees	**-**	-	(900)
Other	**1**	-	(40)
Net cash from activities in financing activities	**(581)**	(2,554)	(1,089)
Increase (decrease) in cash and cash equivalents	**(7,827)**	(20,099)	18,892
Balance of cash at beginning of year	**45,460**	65,684	46,241
Effect of exchange rate changes on cash balances	**(619)**	(125)	551
Balance of cash and cash equivalents at end of year	**37,014**	45,460	65,684

(1) Figures for 2012 and 2011 do not include Leumi Mortgage which was merged with the Bank in 2013.

Interest and taxes paid and/or received and dividends received

	2013	2012	2011 (1)
	(NIS millions)		
Interest received	**10,912**	10,939	10,649
Interest paid	**(5,242)**	(5,798)	(5,024)
Dividends received	**137**	136	480
Taxes paid on income	**(1,036)**	(785)	(670)

D. Information on the basis of historical nominal values for tax purposes

	31 December 2013	31 December 2012
	(NIS millions)	
Total assets	**341,344**	338,602
Total liabilities	**316,285**	315,321
Shareholders' equity	**25,059**	23,281
Net profit (1)	**2,379**	1,087

(a) Not including profits (losses) of companies included on equity basis, as required under generally accepted accounting principles in Israel.

CONDENSED FINANCIAL STATEMENTS
OF PRINCIPAL CONSOLIDATED COMPANIES

Bank Leumi USA

Chairman of the Board: D. Brodet

President and Chief Executive Officer: A. Mendelson[1]

Condensed Consolidated Balance Sheet as at 31 December 2013 (US$ millions)

	2013	2012		2013	2012
Assets			**Liabilities and equity**		
Cash and deposits with banks	**520**	687	Deposits	**4,422**	4,546
Securities	**711**	698	Other liabilities	**132**	189
Loans	**3,678**	3,705	Capital notes	**90**	90
Buildings and equipment	**36**	22			
Other assets	**246**	253	Capital resources	**547**	540
Total assets	**5,191**	5,365	Total liabilities and capital resources	**5,191**	5,365

Condensed Statement of Profit and Loss for the year ended 31 December 2013 (US$ millions)

	2013	2012
Interest income, net	**136**	133
Expenses in respect of credit losses	**11**	7
Profit from interest income, net after allowance for credit losses	**125**	126
Non-interest income	**42**	49
Operating and other expenses	**148**	137
Profit before taxes	**19**	38
Provision for taxes	**8**	14
Net profit	**11**	24

(1) Began serving on 1 September 2013. Until this date, the position was held by Mr. I. Eyal.

Leumi Private Bank[1]
Chairperson of the Board: Prof. D. Tsiddon[2]
Chief Executive Officer: A. Zilberberg[3]

Condensed Consolidated Balance Sheet as at 31 December 2013 (CHF millions)

	2013	2012		2013	2012
Assets			**Liabilities and equity**		
Cash and deposits with banks	**902**	872	Deposits from banks	**14**	38
Loans	**492**	736	Deposits and other accounts	**1,406**	1,577
Securities	**291**	260	Subordinated notes	**50**	50
Other assets	**26**	34	Capital resources and reserves	**241**	237
Total assets	**1,711**	1,902	Total liabilities and capital resources	**1,711**	1,902
Customer investments (off-balance sheet)	**5,162**	5,565			

Condensed Statement of Profit and Loss for the year ended 31 December 2013 (CHF millions)

	2013	2012
Interest income, net	**15**	17
Non-interest income	**65**	66
Operating and other expenses	**68**	82
Profit before taxes	**12**	1
Provision for taxes	**5**	1
Net profit	**7**	-

(1) Until 3 January 2012, the name of the Bank was Bank Leumi (Switzerland) Ltd.
(2) Began serving on 20 February 2014. Until this date, the position was held by Ms. G. Maor.
(3) Began serving on 1 July 2013. Until this date, the position was held by Mr. A. Zaidenberg.

Bank Leumi (UK) plc
Chairman of the Board: Y. Minz(1)
Chief Executive Officer: L. Weiss

Condensed Consolidated Balance Sheet as at 31 December 2013 (£ millions)

	2013	2012		2013	2012
Assets			**Liabilities and equity**		
Cash and deposits with banks	**290**	201	Deposits	**1,327**	1,235
Loans	**1,244**	1,298	Deposits from banks	**55**	150
Securities	**64**	102	Subordinated notes	**84**	84
Equipment and buildings	**6**	6	Other liabilities	**19**	11
Other assets	**10**	7	Capital resources	**129**	134
Total assets	**1,614**	1,614	Total liabilities and capital resources	**1,614**	1,614

Condensed Statement of Profit and Loss for the year ended 31 December 2013 (£ millions)

	2013	2012
Non-interest income	**42**	38
Expenses in respect of credit losses	**34**	18
Inierest income, net after allowance for credit losses	**8**	20
Non-interest income	**14**	14
Operating and other expenses	**29**	28
Profit (loss) before taxes	**(7)**	6
Provision for (benefit from) taxes	**(2)**	1
Net profit (loss)	**(5)**	5

(1) Began serving on 6 March 2013. Until this date, the position was held by Mr. Z. Itskovitch.

Bank Leumi (Luxembourg) S.A.
Chairman of the Board: Prof. D. Tsiddon[(1)]
General Manager: G. Karni

Condensed Consolidated Balance Sheet as at 31 December 2013 (€ millions)

	2013	2012		2013	2012
Assets			**Liabilities and equity**		
Cash and deposits with banks	**404**	347	Deposits of the public	**312**	397
Securities	**28**	29	Deposits from banks	**171**	29
Credit to the public	**93**	92	Other liabilities	**3**	5
Other assets	**4**	5	Total liabilities	**486**	431
			Shareholders' equity	**43**	42
Total assets	**529**	473	Total liabilities and shareholders' equity	**529**	473

Condensed Statement of Profit and Loss for the year ended 31 December 2013 (€ millions)

	2013	2012
Net interest income	**5**	6
Non-interest income	**6**	6
Operating and other expenses	**8**	8
Profit before taxes	**3**	4
Provision for taxes	**-**	-
Net profit	**3**	4

(1) Began serving on 10 March 2014. Until this date the position was held by Prof. N. Trachtenberg.

Bank Leumi Romania S.A.
Chairman of the Board: Y. Minz(1)
Executive President: L. Mitrache

Condensed Consolidated Balance Sheet as at 31 December 2013 (RON millions)*

	2013	2012		2013	2012
Assets			**Liabilitities and equity**		
Cash and deposits in banks	**266**	161	Deposits	**665**	614
Loans	**797**	775	Deposits from banks	**301**	304
Securities	**110**	186			
Equipment and buildings	**19**	19	Other liabilities	**5**	8
Other assets	**6**	9	Capital resources	**227**	224
Total assets	**1,198**	1,150	Total liabilities and capital resources	**1,198**	1,150

Condensed Statement of Profit and Loss for the year ended 31 December 2013 (RON millions)*

	2013	2012
Net interest income	**45**	49
Expenses in respect of credit losses	**7**	4
Net interest income after expenses in respect of credit losses	**38**	45
Non-interest income	**19**	21
Operating and other expenses	**55**	55
Profit before taxes	**2**	11
Tax expense (benefit)	**-**	3
Net profit	**2**	14

* 1 RON = NIS 1.0659.

(1) Began serving on 6 March 2013. Until this date, the position was held by Mr. Z. Itskovitch.

Arab Israel Bank Ltd.

Chairman of the Board: Z. Nahari
Chief Executive Officer: D. Gitter

Condensed Consolidated Balance Sheet as at 31 December 2013 (NIS millions)

	2013	2012		2013	2012
Assets			**Liabilities and equity**		
Cash and deposits with banks	**1,679**	1,467	Deposits of the public	**4,593**	4,345
Securities	**460**	398	Deposits from banks	**1,346**	824
Credit to the public	**4,640**	4,147	Subordinated notes	**104**	157
Allowance for credit losses	**(59)**	(54)	Other liabilities	**273**	251
Credit to the public, net	**4,581**	4,093			
Buildings and equipment	**73**	69	Total liabilities	**6,316**	5,577
Other assets	**76**	77	Equity	**553**	527
Total assets	**6,869**	6,104	Total liabilities and equity	**6,869**	6,104

Condensed Statement of Profit and Loss for the year ended 31 December 2013 (NIS millions)

	2013	2012
Net interest income	**294**	283
Expenses in respect of credit losses	**9**	15
Net interest income after expenses in respect of credit losses	**285**	268
Non-interest income	**128**	123
Operating and other expenses	**249**	233
Profit before taxes	**164**	158
Provision for taxes	**58**	55
Net profit	**106**	103
Dividend paid	**80**	-

Leumi Card Ltd.
Chairman of the Board: T. Yassur
Chief Executive Officer: H. Heller

Condensed Consolidated Balance Sheet as at 31 December 2013 (NIS millions)

Assets	2013	2012	Liabilities and equity	2013	2012
Cash and deposits with banks	**59**	42	Credit from banking corporations	**1,902**	1,596
Receivables in respect of credit card activity	**9,483**	8,780	Payables in respect of credit card activity	**6,254**	6,010
Allowance for credit losses	**(72)**	(72)	Other liabilities	**161**	162
Receivables in respect of credit card activity, net	**9,411**	8,708	Total liabilities	**8,317**	7,768
Investment in companies included on equity basis and others	**2**	1	Equity	**1,402**	1,232
Equipment	**194**	190			
Other assets	**53**	59			
Total assets	**9,719**	9,000	Total liabilities and equity	**9,719**	9,000

Condensed Statement of Profit and Loss for the year ended 31 December 2013 (NIS millions)

	2013	2012
Income from credit card transactions	**830**	795
Net interest income	**154**	156
Other income	**3**	3
Expenses in respect of credit losses	**10**	19
Operating and other expenses	**705**	688
Profit before taxes	**272**	247
Provision for taxes on profit	**76**	69
Profit after taxes	**196**	178
Company's equity in profits after the effect of taxes of companies included on equity basis	**4**	2
Net profit	**200**	180
Dividend paid	**30**	40

Leumi Partners Ltd.
Chairman of the Board: Prof. D. Tsiddon
Chief Executive Officer: Y. Bloch

Condensed Consolidated Balance Sheet as at 31 December 2013 (NIS millions)

	2013	2012		2013	2012
Assets			**Liabilities and equity**		
Cash and deposits with banks	**262**	68			
Securities	**1,222**	1,130	Other liabilities	**35**	22
Deposits in banks	**3**	3			
Investment in investee companies	**420**	441			
Fixed assets	**3**	4	Capital notes	**1,158**	1,154
Other assets	**4**	3	Equity	**721**	473
Total assets	**1,914**	1,649	Total liabilities and equity	**1,914**	1,649

Condensed Statement of Profit and Loss for the year ended 31 December 2013 (NIS millions)

	2013	2012
Net interest income	**(6)**	(2)
Non-interest income	**242**	(42)
Operating and other expenses	**40**	34
Profit before taxes	**196**	(78)
Provision for (benefit from) taxes	**3**	(3)
Profit (loss) after taxes	**193**	(75)
Company's equity in the net profits of companies included on equity basis	**33**	32
Net profit (loss)	**226**	(43)

Leumi Finance Company Ltd.
Chairman of the Board: Y. Marmari
Chief Executive Officer: O. Shlosman

Condensed Consolidated Balance Sheet as at 31 December 2013 (NIS millions) [1]

	2013	2012		2013	2012
Assets			**Liabilities and equity**		
Cash and deposits in banks	**19,063**	20,851	Debentures and subordinated notes	**18,906**	20,693
			Equity	**157**	158
Total assets	**19,063**	20,851	Total liabilities and equity	**19,063**	20,851

Condensed Statement of Profit and Loss for the year ended 31 December 2013 (NIS millions)

	2013	2012
Net interest income	**23**	25
Non-interest income	**3**	5
Profit before taxes	**20**	20
Provision for taxes	**8**	8
Net profit	**12**	12
Dividend paid	**13**	12

(1) The financial statements have been prepared by the company in accordance with International Financial Reporting Standards (IFRS).
(2) Began serving on 22 May 2013. Until this date, the position was held by Mr. M. Aisenthal.

Leumi-Tech Ltd.[1]

Chairman of the Board: Prof. D. Tsiddon[2]

Chief Executive Officer: J. Zaidman Oron[3]

Condensed Consolidated Balance Sheet as at 31 December 2013 (NIS millions)

	2013	2012		2013	2012
Assets			**Liabilities and equity**		
Cash and deposits in banks	**53**	379	Deposits from banks	**41**	79
Credit to the public	**381**	658	Other liabilities	**3**	2
T-bills	**590**	-	Total liabilities	**44**	81
Other assets	**11**	12	Equity	**991**	968
Total assets	**1,035**	1,049	Total liabilities and equity	**1,035**	1,049

Condensed Statement of Profit and Loss for the year ended 31 December 2013 (NIS millions)

	2013	2012
Net interest income	**31**	46
Expenses in respect of credit losses	**-**	2
Net interest income after expenses for credit losses	**31**	44
Non-interest income	**5**	2
Operating expenses	**8**	10
Profit before taxes	**28**	36
Provision for taxes	**5**	9
Net profit	**23**	27

(1) The name of the company was changed on 31 December 2013. Until that date the name of the company was Leumi Leasing & Investments Ltd.
(2) Began serving on 10 February 2013. Until this date, the position was held by Mr. E. Katsav.
(3) Began serving on 1 January 2014. Until this date the position was held by Mr. Y. Weizmann.