Bank Leumi

Risk Management Report

As at December 31 2017

The Risk Management Report and description of the main characteristics of regulatory capital instruments issued appear on the Bank's website at: www.leumi.co.il About > Financial Information > Disclosure under Pillar 3 of the Basel Accord and additional information on risks, and on the Israel Securities Authority's MAGNA website. at www.magna.isa.gov.il

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Risk Management Report

We are pleased to present the Risk Management Report as at December 31 2017 (hereinafter: the "Risk Management Report"). The Risk Management Report has been prepared in accordance with the directives and guidance of the Supervisor of Banks regarding the disclosure requirements outlined in Pillar 3 of the Basel Accord and includes additional risk information.

This report includes information that supplements, and is related to, the consolidated financial statements of Bank Leumi of Israel Ltd. regarding risk exposure and management and capital adequacy. This report should be read with the Report of the Board of Directors and Management and the financial statements as at December 31 2017.

David Brodet
Chairman of the Board

Rakefet Russak-Aminoach
President and CEO

Bosmat Ben-Zvi
First Executive VP
Head of the Risk Management Division

March 5 2018

Purpose and disclosure principle

The purpose of this report is to enable users to evaluate significant information included therein regarding the implementation of the Basel Committee working framework, capital, risk exposure, and risk assessment processes.

The information in this report includes:

- Disclosure requirements published by the Basel Committee (Pillar 3 disclosure requirements).
- Risk disclosure requirements based on other sources, including disclosure requirements published by the Financial Stability Board (FSB) via the Enhanced Disclosure Task Force (EDTF).
- Additional disclosure requirements pursuant to the Bank of Israel’s reporting directives and guidance (additional information).

In order to indicate the origin of the various disclosures, the report includes an index of the various disclosure tables, which denote the origin of the disclosure as either Pillar 3 or EDTF, respectively.

The report was prepared according to the following principles:

- Regarding quantitative data included in previous disclosures under the Pillar 3 disclosure requirements or other disclosure requirements as mentioned above, comparative data have been provided for the previous reporting year, as prescribed by the directives.
- The information is partially based on the financial data presented in the Bank's financial statements, which are used as the basis for calculating regulatory ratios - with the necessary adjustments - and partially on internal assessments and models. As a result, some of the information constitutes unaudited estimates and/or represents information which is considered forward-looking.
- Qualitative information is mostly detailed in this report. Additional relevant information may be found under Risk Review in the 2017 Report of the Board of Directors and Management.

Forward-looking information

The Risk Management Report includes, in addition to data relating to the past, information and assessments relating to the future, defined in the Securities Law, 1968, as "forward-looking information." Forward-looking information relates to a future event or matter, the realization of which is uncertain and not under the Bank's exclusive control.

Forward-looking information is generally worded using the following words or phrases: "the Bank believes", "the Bank foresees", "the Bank expects", "the Bank intends", "the Bank plans", "the Bank estimates", "the Bank's policy", "the Bank's plans", "the Bank's forecast", "expected", "strategy", “targets", "likely to impact", "scenarios", "stress scenarios", " assessment", and additional phrases indicating that the matter in question is a forecast of the future rather than past facts.

Forward-looking information included in the Risk Management Report is based, inter alia, on forecasts of various matters related to economic developments in Israel and abroad, especially the currency markets and capital markets, legislation, regulators’ directives, competitors’ behavior, technological developments and human resources issues.

As a result of the inability to foresee with certainty that these forecasts are realized, and the fact that in reality events may differ from those forecasted, users should treat information defined as "forward-looking" with caution, since reliance on such information involves risk and uncertainty and the future financial and business results of the Leumi Group may be materially different.

The Bank does not undertake to publish updates on forward-looking information included in its reports. This does not derogate from the Bank's reporting obligations according to any law.

List of disclosure Tables

Scope

a. The Group is regulated by the Supervisor of Banks of the Bank of Israel on a consolidated basis. The consolidation of the consolidated companies and the recording of the associates' book value are in accordance with the generally accepted accounting principles and the Bank of Israel's directives. As at December 31 2017, there were no differences between the consolidation basis according to the accounting principles and the regulatory consolidation basis for capital adequacy purposes. The report was prepared in accordance with the requirements of the Basel Committee, and is based on the financial data presented in the financial statements; however, in some cases, the data is different – for example, in respect of capital deductions banks are required to implement, special treatment of the accounting effect of the efficiency plan on the Bank's capital and an adjusted calculation in respect of extraordinary actuarial liabilities.

b. The banking Group's foreign offices are regulated by the respective regulators in their countries of operation, most of which have adopted the Basel Committee's working framework, with certain changes pertaining to capital adequacy, liquidity and leverage requirements.

c. The main regulatory restrictions on the transfer of liquid means or regulatory capital between the Group's companies in Israel and abroad are as follows:

1. The Bank of Israel does not restrict the Bank's deposits with the Group's subsidiaries in Israel and abroad but has imposed restrictions on the Bank's capital investments in foreign companies abroad. Any increase in investment or a decrease in holding any type of means of control to less than 80% requires prior approval by the Bank of Israel.
2. The US subsidiary - The US authorities restrict local banks from any type and extent of exposure to related companies. The maximum allowed exposure rate to a related company is 10% of the Bank's equity capital in the United States, and the US subsidiary's maximum allowed exposure to the Group is 20% of its equity capital.
3. The UK subsidiary (BLUK) - The UK authorities restrict local banks from any type and extent of exposure to related companies. BLUK's maximum rate of exposure to the Group's companies (excluding Bank Leumi of Israel Ltd.) is 25% of the UK Bank's equity.
   Under a waiver issued by the British regulator, the UK subsidiary may increase its exposure to Bank Leumi of Israel Ltd. to 100% of the Bank's equity capital in England.
4. The Romania subsidiary - The UK authorities restrict local banks' exposure to related companies. The Romanian bank's maximum rate of exposure to the Group's companies - including Bank Leumi of Israel Ltd. - is 25% of the Romanian bank's equity capital.

For more information regarding investee companies, please see "Principal investee companies" in Board of Directors Report and Management and Note 15 to the Financial Statements.

Description of the Leumi Group's business

Bank Leumi of Israel Ltd. (hereinafter: "Bank Leumi" or the "Bank"), whose headquarters are located in Tel Aviv, Israel, is the parent company of the Leumi Group (hereinafter: "Leumi" or the "Group"), which controls several major companies, as outlined in the Group Structure chart of the Corporate Governance Report. Bank Leumi and its subsidiary companies constitute one of Israel's largest banking groups.

The Bank is defined as a banking corporation under the Banking (Licensing) Law, 1981, and holds a banking license pursuant to said law. As a banking corporation, Bank Leumi is regulated and restricted by a system of laws, ordinances 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 the Supervisor of Banks' directives, rules, guidance and position papers.

As a leading banking group in Israel, and in order to achieve adequate profitability over time, Leumi constantly examines the trends and changes in the business environment in which it operates and develops strategies that address these changes.

The Group's policy in Israel and around the world is to provide its customers with comprehensive banking and financial solutions and high-level professional service and to enable them to use multiple distribution channels and to offer them a wide range of products tailored to their needs. To implement this strategy, the Bank is organized into three main business lines, each focusing on a different market segment.

For more information, please see "General Review, Goals and Strategy" in the Report of the Board of Directors and Management.

Risk management at Leumi - key metrics

Table 1 - Summary of regulatory ratios and key financial data

	December 31	
	2017	2016
	in NIS millions	
Common equity Tier 1 capital[(a)]	**34,653**	32,586
Total capital[(a)]	**45,541**	44,436
Credit risk[(a)]	**277,344**	266,534
Market risk	**4,464**	4,788
Operational risk	**21,484**	20,843
Total risk-weighted assets	**303,292**	292,165
	in %	
Ratio of common equity Tier 1 capital to risk-adjusted assets[(b)]	**11.43%**	11.15%
Ratio of total capital to risk-adjusted assets[(b)]	**15.02%**	15.21%
Liquidity coverage ratio[(c)]	**122%**	132%
Leverage ratio[(a)]	**6.94%**	6.77%
Ratio of the balance of the allowance for loan losses in respect of loans to the public to the balance of impaired loans to the public	**128.4%**	109.0%
Ratio of problem debt to portfolio of total loans to the public	**2.5%**	2.9%
Balance of the allowance for loan losses out of net loans to the public	**1.4%**	1.5%
Return on equity	**9.8%**	9.3%

(a) These data include adjustments for the efficiency plans prescribed in the Supervisor of Banks' letter dated January 12 2016, *Operational Efficiency of the Banking System in Israel* (hereinafter: "Adjustments for the efficiency plans"). According to the said letter, the reliefs granted in respect of capital adequacy ratios and leverage ratio for the efficiency plans, which were approved by the Board of Directors in June 2016 and in July 2017, are being gradually withdrawn until June 30 2021 and June 30 2022, respectively. For more information regarding the effect of the transitional provisions and adjustments for the efficiency plans, please see "Relief in respect of operational efficiency plans" as well as a table on this subject under "Capital Adequacy" below. Of the total weighted balances of risk-adjusted assets, NIS 94 million was deducted in respect of adjustments for the efficiency plans (on December 31 2016 - NIS 116 million).

(b) The minimum Tier 1 capital ratio and minimum total capital ratio required from January 1 2015 to December 31 2016 are 9% and 12.5%, respectively, and as of January 1 2017 - 10% and 13.5%, respectively. In addition to the above ratios, there is a capital requirement of 1% of the balance of housing loans as at the reporting date. This requirement was gradually implemented in equal quarterly rates from April 1 2015 to January 1 2017. Thus, the minimum Tier 1 capital ratio requirement and the minimum total capital ratio requirement as at the reporting date are 10.25% and 13.75%, respectively.

(c) The Bank's liquidity coverage ratio was calculated according to average daily observations during the reported quarter.

Capital (Pillar 3)

Capital structure (Pillar 3)

Capital attributable to the Bank's equity holders totaled NIS 33,167 million on December 31 2017 compared with NIS 31,347 million as at the end of 2016, a 5.8% year-on-year increase. The increase is mainly due to the net income for the period, which was offset by a net other comprehensive loss and dividend distribution during the year.

This capital serves as the basis for calculating the regulatory capital which, in turn, is used to calculate the Bank's capital adequacy ratio with the addition of capital instruments and regulatory adjustments as set out in the Supervisor of Banks, Proper Conduct of Banking Business Directive No. 202.

Shareholders' equity ratio reached 7.4% at December 31 2017, compared with 7.1% at December 31 2016.

Regulatory capital structure

In May 2013, the Supervisor of Banks published the final directives for the implementation of Basel III in Israel, by amending Proper Conduct of Banking Business Directives Nos. 201-211. The directives went into effect on January 1 2014, subject to the transitional provisions included in the Supervisor of Banks, Proper Conduct of Banking Business Directive No. 299.

Pursuant to the directives, the Group's capital components for the purpose of calculating capital adequacy are attributed to two tiers:

1. Tier 1 Capital, including Common Equity Tier 1 Capital (CET1) and Additional Tier 1 Capital.
2. Tier 2 Capital.

The sum of these tiers is called the "capital basis for capital adequacy" or "regulatory capital" or "total capital".

Tier 1 Capital and Additional Tier 1 Capital.

Common Equity Tier 1 capital includes the capital attributable to the shareholders of the banking corporation, with the addition of some of the minority interests (non-controlling interests of consolidated subsidiaries) less goodwill, other intangible assets and regulatory adjustments and additional deductions, pursuant to Proper Conduct of Banking Business Directive No. 202, *Measurement and Capital Adequacy – Regulatory Capital* and pursuant to the transitional provisions of Proper Conduct of Banking Business Directive No. 299, *Measurement and Capital Adequacy – Regulatory Capital – Transitional Provisions*.

Additional adjustments to Common Equity Tier 1 capital arising from the implementation of operational efficiency plans and the method of calculating the discount rate used to calculate the employee benefits liability, as detailed below.

Additional Tier 1 capital includes capital instruments complying with the criteria set forth in Proper Conduct of Banking Business Directive No. 202. The Leumi Group has no capital instruments in this tier. Any Additional Tier 1 capital instruments which may be issued in the future will be required to comply with all the criteria set forth in Proper Conduct of Banking Business Directive No. 202.

Tier 2 capital

Tier 2 capital mainly includes capital instruments and the balance of the collective credit loss allowance before the related tax effect, up to a maximum of 1.25% of total credit risk-weighted assets.

Capital instruments included in Tier 2 capital at December 31 2013, are subject to transitional provisions and a recognition ceiling, such that the amount actually recognized in respect thereof is the lower of the amortized amount of the instruments and the recognition ceiling based on the balance of capital instruments included in Tier 2 capital as at December 31 2013, which is amortized at the beginning of each year by 10% until January 1 2022. The recognition ceiling for 2017 is 50%.

From the beginning of 2014, capital instruments must comply with the criteria set forth in Proper Conduct of Banking Business Directive No. 202 in order to be included in capital. The main criteria are that the instrument must include: (1) a mechanism for absorbing reserve losses by way of conversion to ordinary shares or amortization of the instrument when the banking corporation's Common Equity Tier 1 capital ratio falls below 5%; (2) a clause determining that, on the occurrence of the defining event for non-viability (as defined in Appendix E to Proper Conduct of Banking Business Directive No. 202), the instrument shall be immediately converted to ordinary shares or written off.

For a description of the main features of regulatory capital instruments which have been issued, please see the Bank's website: www.leumi.co.il under About us > Financial information > Disclosure under Pillar 3 of the Basel Accord and Additional Information on Risks.

Restrictions on capital structure

The following restrictions were provided in Proper Conduct of Banking Directive No. 202:

- Tier 2 capital may not exceed 100% of Tier 1 capital, after the required deductions from this capital.
- Capital instruments qualified to be included in Tier 2 capital may not exceed 50% of Tier 1 capital after the required deductions from Tier 1 capital. This restriction does not include the capital instruments included in Upper Tier 2 capital prior to the Directive's issue, at the balance of those instruments as at December 31 2013, and pursuant to the transitional provisions set forth in Proper Conduct of Banking Business Directive No. 299, *Measurement and Capital Adequacy - Regulatory Capital – Transitional Provisions*.

Table 2 - Composition of capital for the calculation of the capital ratios (Pillar 3)

	December 31	
	2017	2016
	in NIS millions	
Capital components for the calculation of capital ratios		
1. Common equity Tier 1 capital[(a)]		
Equity attributable to the Bank's shareholders	**33,167**	31,347
Differences between the equity attributable to the Bank's shareholders and Common Equity Tier 1 Capital - minority interests	**229**	245
Differences between the equity attributable to the Bank's shareholders and Common Equity Tier 1 Capital - for employee benefits	**590**	868
Adjustments in respect of the transition between the accounting yield curve and the 8-quarter average yield curve[(b)]	**532**	137
Total Common Equity Tier 1 capital before regulatory adjustments and deductions	**34,518**	32,597
Regulatory adjustments and deductions:		
Goodwill and intangible assets	**(203)**	(265)
Deferred taxes receivable	**(219)**	(120)
Regulatory adjustments and other deductions - Common Equity Tier 1 Capital	**(35)**	(19)
Total regulatory adjustments and deductions - Common Equity Tier 1 Capital	**(457)**	(404)
Total adjustments in respect of the efficiency plans[(a)]	**592**	393
Total Common Equity Tier 1 capital after regulatory adjustments and	**34,653**	32,586
2. Tier 2 capital		
Tier 2 capital: instruments before deductions	**7,773**	8,662
Tier 2 capital: allowances before deductions	**3,115**	3,188
Total Tier 2 capital before deductions	**10,888**	11,850
Deductions:		
Total deductions - Tier 2 capital	**-**	-
Total Tier 2 capital	**10,888**	11,850
Total capital	**45,541**	44,436

(a) These data include adjustments for the efficiency plans prescribed in the Supervisor of Banks' letter dated January 12 2016, *Operational Efficiency of the Banking System in Israel* (hereinafter: "Adjustments for the efficiency plans"). According to the said letter, the reliefs granted in respect of capital adequacy ratios and leverage ratio for the efficiency plans, which were approved by the Board of Directors in June 2016 and in July 2017, are being gradually withdrawn until June 30 2021 and June 30 2022, respectively. For more information regarding the effect of the transitional provisions and adjustments for the efficiency plans, please see "Relief in respect of operational efficiency plans" as well as a table on this subject under "Capital Adequacy" below. Of the total weighted balances of risk-adjusted assets, NIS 94 million was deducted in respect of adjustments for the efficiency plans (on December 31 2016 - NIS 116 million).

(b) According to individual approval from the Supervisor of Banks.

Table 3 - Composition of regulatory capital, with references to the regulatory balance sheet (Pillar 3)

	December 31 2017		December 31 2016		
	Regulatory capital	Amounts not deducted from capital subject to the required treatment prior to the adoption of Directive 202 according to Basel III	Regulatory capital	Amounts not deducted from capital subject to the required treatment prior to the adoption of Directive 202 according to Basel III	Reference to the regulatory balance sheet
	in NIS millions				
Common Equity Tier 1 capital: instruments and retained earnings					
Ordinary share capital issued by the banking corporation and premium on ordinary shares included in Common Equity Tier 1 capital	**8,839**	**-**	8,831	-	1
Retained earnings, including dividend proposed or declared after the balance sheet date	**27,341**	**-**	24,792	-	2
Accumulated other comprehensive income and retained earnings that were disclosed	**(2,423)**	**(590)**	(1,408)	(868)	3
Common Equity Tier 1 capital instruments issued by the banking corporation eligible for inclusion in the regulatory capital in the transition period	**-**	**-**	-	-	-
Existing capital injections from the public sector to be recognized by January 1 2018	**-**	**-**	-	-	-
Ordinary shares issued by subsidiaries of the banking corporation (minority interests) which were consolidated and are held by a third party	**229**	**39**	245	81	4
Common Equity Tier 1 capital before regulatory adjustments and deductions	**33,986**	**-**	32,460	-	-
Common Equity Tier 1 capital: regulatory adjustments and deductions					
Stabilization adjustments of valuation purposes	**-**	**-**	-	-	-
Goodwill	**203**	**-**	265	-	6
Other intangible assets excluding mortgage servicing rights, less deferred taxes payable	**-**	**-**	-	-	7
Deferred taxes receivable whose use depends on the banking corporation's future profitability	**2**	**-**	1	1	8

Total accumulated other comprehensive income in respect of cash flow hedges of items not presented in the balance sheet at fair value	**-**	**-**	-	-	-
Negative gap between allowances and expected losses	**-**	**-**	-	-	-
Increase in shareholders' equity arising from securitization transactions	**-**	**-**	-	-	-
Unrealized profits and losses resulting from changes in the fair value of liabilities arising from changes in the banking corporation’s own credit risk.	**35**	**9**	19	13	9
Excess in fund over reserve, less deferred taxes payable that will be settled if the asset becomes impaired or derecognized pursuant to the Reporting to the Public Directives.	**-**	**-**	-	-	-

	December 31 2017		December 31 2016		
	Regulatory capital	Amounts not deducted from capital subject to the required treatment prior to the adoption of Directive 202 according to Basel III	Regulatory capital	Amounts not deducted from capital subject to the required treatment prior to the adoption of Directive 202 according to Basel III	Reference to the regulatory balance sheet
	in NIS millions				
Buyback of ordinary shares, held directly or indirectly (including commitment to purchase shares under contractual agreements).	**-**	**-**	-	-	-
Mutual cross-holdings of ordinary	**-**	**-**	-	-	-
Investments in equity of financial corporations that are not consolidated in the banking corporation's reports to the public, where the banking corporation's stake does not exceed 10% of the ordinary share capital issued by the financial corporation (in an amount exceeding 10% of the Common Equity Tier 1 capital)	**-**	**-**	-	-	-
Investments in the equity of financial corporations that are not consolidated in the banking corporation's reports to the public, where the banking corporation's stake exceeds 10% of the ordinary share capital issued by the financial corporation	**-**	**-**	-	-	-
Mortgage servicing rights whose total exceeds 10% of the Common Equity Tier 1 capital	**-**	**-**	-	-	-
Deferred taxes receivable incurred as a result of timing differences, whose total exceeds 10% of the Common Equity Tier 1 capital	**1,680**	**420**	1,045	696	10
Total mortgage servicing rights, deferred taxes receivable created as a result of timing differences and investments exceeding 10% of the ordinary share capital issued by financial corporations, which exceed 15% of the Common Equity Tier 1 capital of the banking corporation	**-**	**-**	-	-	-
Of which investments exceeding 10% of the ordinary share capital issued by financial corporations	**-**	**-**	-	-	-
Of which: mortgage servicing rights	**-**	**-**	-	-	-

Of which: deferred taxes receivable incurred as a result of timing differences	**-**	**-**	-	-	-
Additional regulatory adjustments and deductions established by the Supervisor of Banks	**(2,588)**	**(312)**	(1,454)	(575)	-
Of which: investments in financial corporations' equity	**-**	**-**	-	-	-
Of which: mortgage servicing rights	**-**	**-**	-	-	-
Of which: calculation of the regulatory capital, based on an eight-quarter average discount rate of the pension obligation	**(749)**	**-**	(199)	-	-
Of which: for the effect of the efficiency plans	**(592)**	**-**	(393)	-	-
Of which: Deduction of salary tax component from deferred tax asset	**(1,247)**	**(312)**	(862)	(575)	-

	December 31 2017		December 31 2016		
	Regulatory capital	Amounts not deducted from capital subject to the required treatment prior to the adoption of Directive 202 according to Basel III	Regulatory capital	Amounts not deducted from capital subject to the required treatment prior to the adoption of Directive 202 according to Basel III	Reference to the regulatory balance sheet
	in NIS millions				
Deductions applicable to Common Equity Tier 1 capital in case there is insufficient capital in Additional Tier 1 capital and Tier 2 capital to cover the deductions	**-**	**-**	-	-	-
Total regulatory adjustments and deductions to Common Equity Tier 1 capital	**(668)**	**-**	(126)	-	-
Common Equity Tier 1 capital	**34,653**	**-**	32,586	-	-
Additional Tier 1 capital: instruments					
Additional Tier 1 share capital instruments issued by the banking corporation and premium on these instruments	**-**	**-**	-	-	-
Of which: classified as share capital pursuant to the Reporting to the Public Directives	**-**	**-**	-	-	-
Of which: classified as liability pursuant to the Reporting to the Public Directives	**-**	**-**	-	-	-
Additional Tier 1 capital: instruments issued by the corporation that are eligible for inclusion in regulatory capital in the transitional period	**-**	**-**	-	-	-
Additional Tier 1 capital instruments issued by subsidiaries of the banking corporation and held by third party investors	**-**	**-**	-	-	-
Of which: additional Tier 1 capital instruments issued by subsidiaries of the banking corporation and held by third party investors that are deducted gradually from Additional Tier 1 capital	**-**	**-**	-	-	-
Additional Tier 1 capital before deductions	**-**	**-**	-	-	-
Additional Tier 1 capital: deductions					
Investment in own capital instruments included in Additional Tier 1 capital, held directly or indirectly (including commitment to purchase instruments under contractual agreements).	**-**	**-**	-	-	-
Mutual cross-holdings of capital	**-**	**-**	-	-	-
Investments in equity of financial corporations not consolidated in the banking corporation's public reports, where the banking corporation's stake does not exceed 10% of the ordinary share capital issued by the financial corporation	**-**	**-**	-	-	-

	December 31 2017		December 31 2016		
	Regulatory capital	Amounts not deducted from capital subject to the required treatment prior to the adoption of Directive 202 according to Basel III	Regulatory capital	Amounts not deducted from capital subject to the required treatment prior to the adoption of Directive 202 according to Basel III	Reference to the regulatory balance sheet
	in NIS millions				
Investments in the equity of financial corporations not consolidated in the banking corporation's public reports, where the banking corporation's stake exceeds 10% of the ordinary share capital issued by the financial corp.	**-**	**-**	-	-	-
Additional deductions established by the Supervisor of Banks	**-**	**-**	-	-	-
Of which: investments in financial corporations' equity	**-**	**-**	-	-	-
Of which: additional deductions for Tier 1 Capital	**-**	**-**	-	-	-
Deductions in Additional Tier 1 capital that are subject to the required treatment prior to the adoption of Directive No. 202 pursuant to Basel III	**-**	**-**	-	-	-
Deductions applicable to Additional Tier 1 capital since there is insufficient Tier 2 capital to cover the deductions	**-**	**-**	-	-	-
Total deductions in Additional Tier 1 capital	**-**	**-**	-	-	-
Additional Tier 1 capital	**-**	**-**	-	-	-
Tier 1 capital	**34,653**	**-**	32,586	-	-
Tier 2 capital: instruments and allowances					
Instruments issued by the banking corporation (that are not included in Common Equity Tier 1 capital) and premium on these instruments	**926**	**-**	926	-	11a
Tier 2 capital instruments issued by the corporation that are eligible for inclusion in regulatory capital in the transitional period	**6,816**	**-**	7,715	-	11
Tier 2 capital instruments issued by subsidiaries of the banking corporation and to third party investors	**31**	**-**	21	-	5
Of which: Tier 2 capital instruments issued by subsidiaries of the banking corporation and held by third party investors that are deducted gradually from Tier 2 capital	**31**	**-**	21	-	-
Collective allowances for credit losses according to the relevant tax effect	**3,115**	**-**	3,188	-	12
Tier 2 capital before deductions	**10,888**	**-**	11,850	-	-
Tier 2 capital: deductions					
Investment in own Tier 2 capital instruments held directly or indirectly (including commitment to purchase instruments under contractual agreements).	**-**	**-**	-	-	-
Mutual cross-holdings of Tier 2 capital instruments of financial corporations	**-**	**-**	-	-	-

	December 31 2017		December 31 2016		
	Regulatory capital	Amounts not deducted from capital subject to mandatory treatment prior to the adoption of Directive 202 according to Basel III	Regulatory capital	Amounts not deducted from capital subject to mandatory treatment prior to the adoption of Directive 202 according to Basel III	Reference to the regulatory balance sheet
	in NIS millions				
Investments in equity of financial corporations not consolidated in the banking corporation's public reports, where the banking corporation's stake does not exceed 10% of the ordinary share capital issued by the financial corporation	**-**	**-**	-	-	**-**
Investments in the equity of financial corporations that are not consolidated in the banking corporation's reports to the public, where the banking corporation's stake exceeds 10% of the ordinary share capital issued by the financial corporation	**-**	**-**	-	-	-
Additional deductions established by the Supervisor of Banks	**-**	**-**	-	-	-
Of which: investments in financial corporations' equity	**-**	**-**	-	-	-
Of which: additional deductions for Tier 2 capital	**-**	**-**	-	-	-
Regulatory adjustments to Tier 2 capital that are subject to the required treatment prior to the adoption of Directive No. 202 pursuant to Basel III					
Total regulatory adjustments and deductions to Common Equity Tier 2 capital	**-**	**-**	-	-	-
Tier 2 capital	**10,888**	**-**	11,850	-	-
Total capital	**45,541**	**-**	44,436	-	-
Total risk assets weighted in accordance with the treatment required before adoption of Directive No. 202 pursuant to Basel III	**108**	**-**	122	-	-
Of which: other deferred tax assets	**108**	**-**	122	-	13
Total risk-weighted assets	**303,292**	**-**	292,165	-	-
Capital ratios and capital conservation buffers					
Common Equity Tier 1 Capital (as a percentage of risk-weighted assets)	**11.43%**	**-**	11.15%	-	-
Tier 1 capital (as a percentage of risk-weighted assets)	**11.43%**	**-**	11.15%	-	-
Total capital (as a percentage of risk-weighted assets)	**15.02%**	**-**	15.21%	-	-
Minimum Common Equity Tier 1 capital determined by the Supervisor of Banks	**10.25%**	**-**	9.24%	-	-
Minimum Tier 1 capital ratio determined by the Supervisor of Banks	**-**	**-**	-	-	-
Minimum total capital ratio determined by the Supervisor of Banks	**13.75%**	**-**	12.74%	-	-

	December 31 2017		December 31 2016		
	Regulatory capital	Amounts not deducted from capital subject to mandatory treatment prior to the adoption of Directive 202 according to Basel III	Regulatory capital	Amounts not deducted from capital subject to mandatory treatment prior to the adoption of Directive 202 according to Basel III	Reference to the regulatory balance sheet
	in NIS millions				
Amounts below the deduction threshold (before risk weighting)					
Investments in equity of financial corporations (excluding banking corporations and their subsidiaries) not exceeding 10% of the ordinary share capital issued by the financial corporation and which are below the deduction threshold	**310**	**-**	455	-	14
Investments in Common Equity Tier 1 capital (excluding banking corporations and their subsidiaries) exceeding 10% of the ordinary share capital issued by the financial corporation and which are below the deduction threshold	**251**	**-**	249	-	15
Mortgage servicing rights	**-**	**-**	-	-	-
Deferred taxes receivable created incurred as a result of timing differences that are below the deduction threshold	**3,471**	**-**	3,262	-	16
Ceiling for including allowances in Tier 2					
Allowance eligible for inclusion in Tier 2 relating to exposures under the standardized approach, prior to implementing the ceiling	**3,115**	**-**	3,188	-	-
Ceiling for inclusion in Tier 2 under the standardized approach	**3,467**	**-**	3,332	-	-
Allowance eligible for inclusion in Tier 2 relating to exposures under the internal ratings-based (IRB) approach, before implementation of the ceiling	**-**	**-**	-	-	-
Ceiling for inclusion in Tier 2 under the internal ratings-based approach	**-**	**-**	-	-	-
Capital instruments not eligible as regulatory capital subject to the transitional provisions					
Amount of the present ceiling for instruments included in Common Equity Tier 1 capital subject to the transitional provisions	**-**	**-**	-	-	-
Amount deducted from Common Equity Tier 1 capital due to the ceiling	**-**	**-**	-	-	-
Amount of present ceiling for instruments included in Additional Tier 1 capital subject to the transitional provision	**-**	**-**	-	-	-
Amount deducted from Additional Tier 1 due to the ceiling	**-**	**-**	-	-	-
Amount of the present ceiling for instruments included in Tier 2 capital subject to the transitional provisions	**7,272**	**-**	8,726	-	-
Amount deducted from Tier 2 capital due to the ceiling	**-**	**-**	-	-	-

Table 4 - Composition of the regulatory balance sheet with references to components of regulatory capital (Pillar 3)

	December 31		References to components of regulatory capital
	2017	2016	
	in NIS millions		
Assets			
Cash and deposits with banks	**82,067**	74,757	-
Securities[1]	**77,299**	77,201	-
Of which: Investments in equity of financial corporations which do not exceed 10% of the financial corporation's equity capital[1]	**310**	455	14
Of which: other securities[1]	**76,989**	76,746	-
Loans to the public	**271,216**	265,450	-
Allowance for loan losses[1]	**(3,264)**	(3,537)	-
Of which: collective allowance for loan losses included in Tier 2[1]	**2,781**	(2,854)	12
Of which: allowance for loan losses not included in regulatory capital[1]	**(483)**	(683)	-
Net loans to the public	**267,952**	261,913	-
Loans to governments	**715**	642	-
Investments in investee companies[1]	**807**	901	-
Of which: investments in the capital of financial corporations exceeding 10% of the financial corporation's equity capital	**251**	249	15
Of which: goodwill[1]	**187**	246	6
Buildings and equipment	**2,986**	3,147	-
Other assets[1]	**8,262**	8,087	-
Of which: deferred tax assets[1, 2]	**5,476**	4,960	-
Of which: deferred tax assets excluding those attributed to timing differences[2]	**2**	1	8
Of which: deferred tax assets in respect of intangible assets[2]	**-**	-	7
Of which: deferred tax assets attributed to timing differences, whose total exceeds 10% of Common Equity Tier 1 capital[2]	**1,680**	1,044	10
Of which: deferred tax assets attributed to timing differences, whose total does not exceed 10% of Common Equity Tier 1 capital[2]	**3,471**	3,262	16
Of which: other deferred tax assets pursuant to the transitional provisions[2]	**323**	652	13
Of which: other assets[1]	**2,786**	3,127	-
Intangible assets and goodwill[1]	**16**	17	-
Of which: goodwill[1]	**16**	17	6
Securities borrowed or purchased under agreements to resell	**1,161**	1,284	-
Assets for derivatives	**9,573**	10,654	-
Total assets	**450,838**	438,603	-

	December 31		References to components of regulatory capital
	2017	2016	
	in NIS millions		
Liabilities and capital			
Deposits by the public	**362,478**	346,854	-
Deposits from banks	**5,156**	3,394	-
Deposits from governments	**452**	900	-
Debentures and subordinated notes[1]	**15,577**	22,640	-
[1]Of which subordinated notes not recognized as regulatory capital	**7,835**	14,000	-
Of which: subordinated notes recognized as regulatory capital[2]	**7,742**	8,640	-
Of which: eligible as regulatory capital components[2]	**926**	926	11a
Of which: eligible as regulatory capital components and subject to transitional provisions[2]	**6,816**	7,714	11
Other liabilities[1]	**23,324**	21,885	-
Of which: collective allowance for loan losses included in Tier 2[1]	**334**	334	12
Securities borrowed or purchased under agreements to resell	**558**	539	-
Liabilities in respect of derivative instruments[1]	**9,740**	10,677	-
Of which: in respect of own credit risk[1]	**43**	32	9
Total liabilities	**417,285**	406,889	-
Non-controlling interests[1]	**386**	367	-
Of which: non-controlling interests attributable to Common Equity Tier 1 Capital[1]	**229**	245	4
Of which: non-controlling interests attributable to Tier 2 Capital[1]	**31**	21	5
Total capital attributed to shareholders of the banking corporation[1]	**33,167**	31,347	-
Of which: ordinary share capital[1]	**7,110**	7,109	1
Of which: premium for ordinary shares[1]	**1,729**	1,722	1
Of which: retained earnings[1]	**27,341**	24,792	2
Of which: Unrealized gains (losses) from adjustment of securities available for sale at fair value[1]	**77**	(84)	3
Of which: net losses from adjustments from translation of financial statements [1]	**(184)**	(53)	3
Of which: other reserves[1]	**44**	30	3
Of which: gains (losses) from adjustments in respect of employee benefits included in regulatory capital [1]	**(2,360)**	(1,301)	3
Of which: Profits (losses) from adjustments in respect of employee benefits not included in regulatory capital[1]	**(590)**	(868)	-
Total shareholders' equity	**33,553**	31,714	
Total liabilities and capital	**450,838**	438,603	

Table 5 - Changes in the composition of regulatory capital (EDTF)

	For the year ended December 31		
	2017	2016	2015
	in NIS millions		
Common Equity Tier 1 capital			
Balance at beginning of period	**32,586**	29,001	27,723
Non-cash issue	**1**	50	-
Increase in premium	**7**	593	-
Net income for the period less dividend	**2,549**	2,791	2,782
Retained earnings reserves in respect of associates	**12**	17	-
Unrealized gains (losses) from adjustments of available for sale securities	**168**	(153)	(327)
Capital reserve for equity-based payment	**-**	(7)	10
Capital reserves in respect of employee benefits	**(1,059)**	(664)	(596)
Increase in (investee and other) capital reserves and reserve for employee benefits	**2**	(73)	13
Effect of the efficiency plans	**124**	308	-
The effect of transitioning to the pension obligation capitalization rate according to an 8-quarter moving average	**395**	137	-
Changes in the translation differences reserve in respect of subsidiaries	**(131)**	-	-
Minority interests	**(16)**	(17)	(40)
Regulatory adjustments and deductions			
Goodwill and intangible assets	**59**	9	(84)
Deferred taxes in respect of that future earnings	**(1)**	1	2
Change in deferred taxes as a result of discounting a pension obligation according to a moving average	**153**	63	-
Change in deferred taxes as a result of the efficiency plans	**71**	84	-
Deferred taxes in respect of timing differences	**(251)**	458	(520)
Accumulated gains/losses arising from changes in own credit risk for financial liabilities at fair value	**(16)**	(13)	(4)
Net increase in Common Equity Tier 1 capital	**2,067**	3,585	1,278
Balance as at end of period	**34,653**	32,586	29,001
Tier 2 capital			
Balance at beginning of year	**11,850**	12,593	14,684
Amortization of subordinated notes pursuant to the transitional provisions	**(899)**	(1,723)	(2,198)
Issuing eligible subordinated notes	**-**	926	-
Minority interests	**10**	9	8
Expenses in respect of the collective allowance	**(73)**	45	99
Net change in Tier 2 capital	**(962)**	(743)	(2,092)
Balance as at end of period	**10,888**	11,850	12,593
Total capital as at the end of period	**45,541**	44,436	41,594

See notes on next page.

Notes:

In 2017, the changes in the regulatory capital arise mainly from a net income for the period less dividends in the amount of NIS 2,549 million; an increase in negative capital reserves for employee benefits in the amount of NIS 1,059 million; an increase in the effect of transitioning to an average curve in the amount of NIS 395 million; a decrease in capital as the result of changes in deferred taxes attributed to timing differences in the amount of NIS 251 million; a decrease in regulatory capital instruments in the amount of NIS 899 million, due to the effect of the decrease in the recognition ceiling from 60% to 50% for these instruments, which are no long eligible and are subject to deduction pursuant to the transitional provisions.

In 2016, the changes in the regulatory capital arose mainly from: a net income for the period in the amount of NIS 2,791 million; an issue of shares to employees and officeholders and related premiums in the amount of NIS 643 million; an increase in negative capital reserves for employee benefits in the amount of NIS 664 million; an increase in capital as a result of the effect of the relief (net of tax) for the efficiency plan approved in June 2016 in the amount of NIS 308 million (according to the Supervisor of Banks' letter dated January 12 2016, Operational Efficiency of Israel's Banking System, recognized over 5 years starting from June 30 2016); an increase in capital as the result of changes in deferred taxes attributed to timing differences in the amount of NIS 458 million; a decrease in regulatory capital instruments in the amount of NIS 1,723 million due to the effect of the decrease in the recognition ceiling from 70% to 60% for these instruments, which are no longer eligible and are subject to deduction pursuant to the transitional provisions; and an increase in regulatory capital instruments deriving from the issue of eligible subordinated notes in the amount of NIS 926 million.

In 2015, the changes in the regulatory capital arose mainly from a net income for the period in the amount of NIS 2,782 million; an increase in negative capital reserves for employee benefits in the amount of NIS 596 million; a decrease in capital as a result of changes in deferred taxes attributed to timing differences in the amount of NIS 520 million; a decrease in regulatory capital instruments in the amount of NIS 2,198 million, due to the effect of the decrease in the recognition ceiling from 80% to 70% for these instruments, which are no longer eligible and are subject to amortization pursuant to the transitional provisions.

For more information on actions taken to improve the capital adequacy, please see further below in this report.

Capital Adequacy (Pillar 3)

The Bank implements the capital measurement and adequacy directives according to the Basel III rules, as adopted by the Supervisor of Banks and incorporated into Proper Conduct of Banking Business Directives Nos. 201-211, as well as their implementation guidelines. The Basel rules require managing capital under three pillars:

- Pillar 1 - includes the mechanism for calculating the minimum regulatory capital requirements for credit risk, operational risk and market risk. In applying Pillar 1 requirements, the Bank implements the standardized approach for all of its exposures and the current exposure approach regarding counterparty exposures.
- Pillar 2 - The Internal Capital Adequacy Assessment Process (ICAAP) outlines the Bank's internal workflows for estimating the required capital in respect of all risks, including those not covered by Tier 1, such as: credit concentration, the banking portfolio's interest risk and pension risk. At the same time, the Supervisor of Banks carries out a review process.
- Pillar 3 - market discipline. The Pillar determines the scope and manner of presenting the information regarding the Bank's risk exposure in its reports to the public. The Pillar requires disclosures included in the Risk Management Report.

The capital ratios are calculated as the ratio of capital to the risk-weighted assets. The Common Equity Tier 1 Capital is calculated as the ratio between Common Equity Tier 1 Capital and the risk-weighted assets, and the total capital ratio is calculated as the ratio of total capital to the risk-weighted assets.

The Bank of Israel's capital adequacy targets

Under Proper Conduct of Banking Business Regulation No. 201, *Capital Measurement and Adequacy - Introduction, Application and Calculation of Requirements*, a large banking corporation whose consolidated balance sheet assets total at least 20% of the Israeli banking system's total balance sheet assets, is required to meet a Common Equity Tier 1 capital ratio of at least 10% and a total capital ratio of at least 13.5%, beginning on January 1 2017. This requirement applies to Leumi.

Additionally, under Amendment to Proper Conduct of Banking Business Directive No. 329, *Restrictions on Granting Housing Loans*, the banking corporation is required to increase its Common Equity Tier 1 Capital target and total capital target by a rate which reflects 1% of the outstanding balance of its housing loans. The requirement was implemented gradually over eight quarters until January 1 2017, with a 0.25% effect on the capital ratio.
As a result, the minimum capital requirements applicable to the Bank as of December 31 2017 are 10.25% for the Common Equity Tier 1 capital ratio and 13.75% for the total capital ratio.

The Bank's capital planning and capital adequacy targets

The Leumi Group's capital planning reflects a forward-looking view of its risk appetite and profile, business strategy and resulting capital adequacy. Capital planning is approved by the Bank's management and Board of Directors and takes into account the various P&L centers of the Group and other factors that affect the Bank's compliance with the capital requirements, such as profit forecasts, changes in other comprehensive income, regulatory adjustments, the effect of the transitional provisions and the rate of increase in risk-weighted assets. The capital ratios forecast is also subjected to various sensitivity tests and stress scenarios.

The Group's policy, which was approved by the Board of Directors, is to maintain a capital adequacy level that is higher than the minimum threshold set by the Bank of Israel from time to time and no less than the rate of capital required to cover the risks as assessed using the ICAAP process. In addition, the Group set targets it would like to meet in case of a stress scenario event.

Under the regulatory review process, the Supervisor of Banks instructed the banks to set internal capital targets that would match each Bank's risk profile. As a result, the Bank's Board of Directors approved an increase in the Bank's internal Tier 1 capital target to 10.5%, as of December 31 2017.

Adjustments to Common Equity Tier 1 capital

Measurement of the employee benefit liability

The employee benefits standard, which was first applied in January 2015, has a material effect on Leumi's Common Equity Tier 1 capital, mainly due to the fact that the liability is measured in accordance with market interest rates which are at historical lows, and also due to the considerable volatility that such measurement generates in the Bank's regulatory capital.

In July 2016, the Bank received individual approval from the Bank of Israel regarding the method of calculating the capitalization interest to be used for calculating the liability for employee benefits for the purpose of measuring regulatory capital. Pursuant to the approval, the calculation of the capitalization interest is based on a moving average of market yields for the eight-quarter period ended on the reporting date. The change is to be implemented from the financial statements for the period ended June 30 2016 to the financial statements as at December 31 2020 (inclusive). The method change significantly moderates the volatility of the Bank's regulatory capital resulting from changes in the capitalization interest rate.

For more information regarding the capitalization methodology, please see Accounting Policies and Estimates on Critical Subjects in the Report of the Board of Directors and Management.

Relief for operational efficiency plans

In January 2016, the Supervisor of Banks published a circular, *Operational Efficiency of the Banking System in Israel*. Pursuant to this circular, a banking corporation which meets the prescribed conditions will be granted a relief, according to which it may spread the effect of the plan on the capital adequacy and leverage ratios on a straight-line basis, over a period of five years.

In June 2016, the Bank's Board of Directors approved an efficiency plan, for a total cost of NIS 438 million (after tax). As of December 31 2017, 30% of the plan's costs are attributable to regulatory capital.

In June 2017, the Supervisor of Banks published an additional letter, *Increasing Operational Efficiency of the Banking System in Israel — Increasing Efficiency in Real Estate*. The letter extended the relief in respect of increasing manpower efficiency to the end of June 2018. In July 2017, the Bank's Board of Directors approved an additional efficiency plan, for a total cost of NIS 204 million (after tax); its effect on capital ratios and the leverage ratio is spread on a straight-line basis over a period of five years. As of December 31 2017, 10% of the plan's costs are attributable to regulatory capital.

Additional regulatory changes

Developments in measuring capital adequacy in the directives of the Basel Committee on Banking Supervision

In December 2017, the Basel Committee on Banking Supervision completed its revision of the overall capital adequacy framework. As part of the revisions, also known as Basel IV, significant revisions were made to the manner of calculating risk-weighted assets for the purpose of the Tier 1 capital requirements. Inter alia, changes were made in the method of calculating capital requirements according to the standardized approach to credit risk, a uniform standardized approach was prescribed with regard to operating risk, and changes were made in the measurement of market risks. Under the rules of the Basel Committee, these changes are due to take effect gradually from January 1 2022 to January 1 2027. Presently, the Bank does not know how and when these rules will be adopted by Israel's Banking Supervision Department.

Capital requirements for exposures to central counterparties

On October 22 2015, the Banking Supervision Department published a circular, *Capital Requirements in respect of Exposures to Central Counterparties*. The circular sets out the new guideline that will apply to exposures to central counterparties caused by OTC derivatives, derivatives traded on the Tel Aviv Stock Exchange and securities financing transactions. At this point, the guidelines do not alter the treatment of the Bank's exposure to customers in respect of derivatives traded on the Tel Aviv Stock Exchange, for which the Bank continues to apply the scenario method.

In July 2017 the Banking Supervision Department approved the Stock Exchange Clearing House and the MAOF Clearing House as counterparties eligible for the purpose of calculating capital requirements in respect of exposure to central counterparties pursuant to Appendix C of Directive No. 203.

For more information, please see Note 25B to the financial statements.

The following is a sensitivity analysis of the main factors affecting the capital adequacy of the Leumi Group:

- A change in the volume of risk-weighted assets – Leumi's risk-weighted assets amounted to NIS 303.3 billion at the end of December 2017. Every 1% increase in risk-weighted assets (about NIS 3 billion) will reduce the Common Equity Tier 1 capital ratio by 0.11%, and the total capital ratio by 0.15%.
- Accrued profit or a change in the capital reserve – Leumi's Common Equity Tier 1 Capital was NIS 34.7 billion at December 31 2017. The total capital amounts to NIS 45.5 billion. Accrual of net income and/or positive change in the capital reserve of each NIS 1 billion will improve the Common Equity Tier 1 Capital ratio and the total capital ratio by 0.33%.
- Liabilities for employee benefits – The actuarial liability for employees is discounted according to an eight-quarter moving average of market yields, which are affected by the Government of Israel's debenture curve and by the U.S. AA corporate debenture spread. A change of 0.1% across the discount

rate curve, under the assumption that the curve rises and falls uniformly, means a cumulative effect of 0.07% on the Common Equity Tier 1 capital ratio and total capital ratio. Of which, according to a moving average calculation for eight quarters, an increase of 0.01% in the Common Equity Tier 1 Capital ratio and the total capital ratio for the current quarter.

The above information regarding capital adequacy and its management refers to the Bank's future activities and constitutes "forward-looking information." For the meaning of the term, please see under “Forward-Looking Information.“

Dividend distribution policy

On March 29 2017, the Bank's Board of Directors approved a dividend distribution policy, effective as of the publication date of the financial statements for the first quarter of 2017. Pursuant to said policy, each quarter, the Bank will distribute a dividend constituting 20% of the Bank's net profit according to the Bank's financial statements for the previous quarter, and subject to, among other things, the Bank complying with its capital adequacy targets after the dividend distribution

On November 20, 2017, the Bank's Board of Directors approved a change in the Bank's dividend distribution policy, under which the Bank will distribute, each quarter, a dividend of up to 40% of the Bank's net income in accordance with the Bank's financial statements for the previous quarter, and subject to, inter alia, the Bank's meeting its capital adequacy targets, even after the dividend distribution. The actual dividend distribution is subject to the specific resolutions of the Board of Directors prior to each distribution, and subject to the provisions of the law which apply to a distribution of dividends, including the provisions of the Companies Law and directives of the Bank of Israel.

In accordance with the revised policy, on March 5 2018, the Board of Directors approved, in respect of Q4 2017, a dividend of 40% of the net income of the quarter. The dividend approved amounted to NIS 342 million, which is 22.416 agorot per share of NIS 1 par value. The Board of Directors determined that March 19 2018 will be the determining date for purposes of payment of the dividend and March 28 2018 will be the payment date. The aggregate dividend in respect of 2017 was NIS 969 million.

Details on paid dividend

Announcement date	Payment date	Dividend per share	Cash dividend
		in agorot	in NIS millions
May 25 2017	June 22 2017	8.168	124
August 15 2017	September 11 2017	11.504	175
November 21 2017	December 21 2017	21.515	328

The Bank's share buyback plan

On March 5 2018, the Bank's Board of Directors approved a plan to buy back the Bank's shares for a total of up to NIS 700 million, from April 1 2018 to March 31 2019. The buy-back is subject to meeting - at each buy-back date - a Tier 1 Equity ratio of no less than 10.9%, in accordance with the most recent financial statements, after having taken into account the buyback plan, and subject to the Bank's three-year capital adequacy planning meeting the differential Tier 1 equity ratio set for the Bank, in addition to a buffer. The Board of Directors believes the buyback plan will allow the Bank to manage its capital in a more efficient way. The buyback plan is subject to the provisions applicable to dividend distribution, including the provisions of the Companies Law and the directives of the Bank of Israel.

For more information, please see the immediate report dated March 6 2018.

Table 6 - Ratio of capital adequacy to risk components

	December 31	
	2017	2016
	in NIS millions	
Capital for calculating capital ratio		
Common Equity Tier 1 Capital, after regulatory adjustments and deductions(a)	**34,653**	32,586
Tier 2 capital, after deductions	**10,888**	11,850
Total capital	**45,541**	44,436
Balance of risk-weighted assets		
Credit risk(a)	**277,344**	266,534
Market risk	**4,464**	4,788
Operational risk	**21,484**	20,843
Total risk-weighted assets	**303,292**	292,165
Ratio of capital to risk components		
Ratio of common equity Tier 1 capital to risk components	**11.43%**	11.15%
Ratio of total capital to risk components	**15.02%**	15.21%
Minimum Common Equity Tier 1 capital ratio set by the Supervisor of Banks(b)	**10.25%**	9.24%
Minimum total equity set by the Supervisor of Banks(b)	**13.75%**	12.74%
Significant subsidiaries:		
Leumi Card:(c)		
Ratio of common equity Tier 1 capital to risk components	**15.80%**	16.81%
Ratio of total capital to risk components	**16.80%**	17.79%
Bank Leumi USA:(d)		
Ratio of common equity Tier 1 capital to risk components	**11.51%**	12.21%
Ratio of total capital to risk components	**13.82%**	14.75%

(a) These data include adjustments for the efficiency plans prescribed in the Supervisor of Banks' letter dated January 12 2016, *Operational Efficiency of the Banking System in Israel* (hereinafter: "Adjustments for the efficiency plans"). According to the said letter, the reliefs granted in respect of capital adequacy ratios and leverage ratio for the efficiency plans, which were approved by the Board of Directors in June 2016 and in July 2017, are being gradually withdrawn until June 30 2021 and June 30 2022, respectively. For more information regarding the effect of the transitional provisions and adjustments for the efficiency plans, please see "Relief in respect of operational efficiency plans" as well as a table on this subject below. Of the total weighted balances of risk-adjusted assets, NIS 94 million was deducted in respect of adjustments for the efficiency plans (on December 31 2016 - NIS 116 million).

(b) The Common Equity Tier 1 capital ratio and minimum total capital ratio required from January 2015 to December 31 2016 are 9% and 12.5%, respectively. These ratios are compounded by a capital requirement representing 1% of the housing loans' outstanding balance as of the reporting date. The requirement was implemented gradually, in equal quarterly rates, from April 1 2015 through January 1 2017. Thus, the minimum Tier 1 capital ratio requirement and the minimum total capital ratio requirement as at the reporting date are 10.25% and 13.75%, respectively.

(c) The capital requirements are in line with those of the Supervisor of Banks: The minimum Common Equity Tier 1 capital ratio and the minimum total capital ratio are 8% and 11.5%, respectively.

(d) The capital requirements are in line with the local regulations which apply to Leumi USA: The minimum Common Equity Tier 1 capital ratio and the minimum total capital ratio are 4.5% and 8%, respectively. As of December 31 2017, these ratios are compounded by a 1.25% capital conservation buffer. The requirement will be implemented gradually until 2019, at which time the capital conservation buffer will be 2.5%.

Effect of the transitional provisions and adjustments for the efficiency plans on the Common Equity Tier 1 capital

	December 31	
	2017	2016
	In %	
Ratio of capital to risk components		
CET1 capital to risk components prior to the implementation of the transitional provisions and before the effect of adjustments for the efficiency plans[(a)]	**11.03%**	10.66%
Effect of the transitional provisions[(b)]	**0.20%**	0.35%
CET1 capital to risk components, before the effect of adjustments for the efficiency plans	**11.23%**	11.01%
Effects of adjustments for the efficiency plans[(c)]	**0.20%**	0.14%
Common equity Tier 1 capital to risk components	**11.43%**	11.15%

(a) Including the effect of adopting the US GAAP on employee rights.
(b) Under the transitional provisions, the Bank takes into account capital deductions and other regulatory adjustments at a gradual increasing rate until full implementation, beginning on January 1 2018.
(c) These data include adjustments for the efficiency plans prescribed in the Supervisor of Banks' letter dated January 12, 2016, Operational Efficiency of the Banking System in Israel. According to the said letter, the reliefs granted in respect of capital adequacy ratios and leverage ratio for the efficiency plans, which were approved by the Board of Directors in June 2016 and in July 2017, are being gradually withdrawn until June 30 2021 and June 30 2022, respectively.

Table 7 - Risk-weighted assets and capital requirements for credit risk, market risk and operational risk (Pillar 3)

Exposures to various risks is measured according to the Bank's book balances, which were prepared in accordance with the GAAP applicable to the Bank and the specific calculation instructions set out in Proper Conduct of Banking Business Directives Nos. 203-209. The method of measurement may change in accordance with changes in these GAAP and other changes, such as: in a portfolio's size and mix, in a portfolio's quality and economic data, and in calculation methods. The following risk exposures are based on the rules set out for the purpose of calculating the regulatory capital required to support these risks.

	Basel III			
	December 31			
	2017		2016	
	Risk-weighted assets	Capital requirement[(a)(b)]	Risk-weighted assets	Capital requirement[(a)(b)]
	in NIS millions			
Risk-weighted assets and capital requirements for credit risk arising from exposures to:				
Sovereign debts	**1,746**	**240**	1,038	133
Debts of public sector entities	**3,518**	**484**	3,381	432
Debts of banking corporations	**4,474**	**615**	3,208	410
Securities	**17**	**40**	173	22
Debts of corporations	**95,739**	**13,164**	94,582	12,078
Debt collateralized by commercial	**54,552**	**7,501**	50,228	6,414
Retail exposures to individuals	**35,740**	**4,914**	35,512	4,535
Loans to small businesses	**13,618**	**1,872**	12,074	1,542
Housing mortgages	**43,519**	**5,984**	43,972	5,615
Securitization	**441**	**61**	490	63
Other assets	**22,031**	**3,029**	20,469	2,614
CVA risk	**1,674**	**230**	1,407	180
Total for credit risk	**277,344**	**38,134**	266,534	34,038
Risk-weighted assets and capital	**4,464**	**614**	4,788	611
Risk-weighted assets and capital	**21,484**	**2,954**	20,843	2,662
Total risk-weighted assets and capital	**303,292**	**41,703**	292,165	37,311

(a) Additional capital buffers have been added in respect of Pillar 2.
(b) The capital requirements were calculated in accordance with the minimum total capital required by the Banking Supervision Department at a rate of 13.75% as at December 31 2017 and 12.74% as at December 31 2016.

Table 8 - Components of risk-weighted assets by business activity (EDTF)

Following is the allocation of risk-weighted assets according to the business lines, as reflected in the Bank's reporting on operating segments.

	December 31 2017										
	Activity in Israel									**Foreign opera= tions**	**Total**
	Households	Private banking	Small- and micro-businesses	Medium-sized businesses	Corpora-tions	Instituti-onals	Financial manage ment	Other	Total Israel		
	in NIS millions										
Credit risk	**71,686**	**411**	**45,788**	**26,928**	**72,009**	**794**	**14,742**	**16,403**	**248,761**	**28,583**	**277,344**
Market risk	**-**	**-**	**-**	**-**	**-**	**-**	**4,416**	**-**	**4,416**	**48**	**4,464**
Operational risk	**6,975**	**450**	**3,622**	**1,802**	**3,116**	**391**	**2,259**	**422**	**19,037**	**2,447**	**21,484**
Total risk-weighted assets	**78,661**	**861**	**49,410**	**28,730**	**75,125**	**1,185**	**21,417**	**16,825**	**272,214**	**31,078**	**303,292**

	December 31 2016(a)										
	Activity in Israel									Foreign opera-tions	Total
	Households	Private banking	Small- and micro-businesses	Medium-sized businesses	Corpora-tions	Instituti-onals	Financial manage ment	Other	Total Israel		
	in NIS millions										
Credit risk	73,055	280	42,835	25,262	68,288	614	11,567	15,588	237,489	29,045	266,534
Market risk	-	-	-	-	-	-	4,705	-	4,705	83	4,788
Operational risk	7,001	475	2,938	2,033	3,209	483	2,033	321	18,493	2,350	20,843
Total risk-weighted assets	80,056	755	45,773	27,295	71,497	1,097	18,305	15,909	260,687	31,478	292,165

(a) Reclassified

Table 9 - Changes in risk-weighted assets (EDTF)

Below are changes in risk-weighted assets arising from changes in mix, credit quality and other reasons that affected their balance in order to calculate the Bank's capital requirements.

Changes in credit risk-weighted assets

	For the year ended December 31		
	2017	2016	2015
	in NIS millions		
Opening balance	**266,534**	277,034	273,881
Change in transactions	**12,117**	(6,550)	6,030
Collateral insurance pursuant to the Sales Law	**81**	(7,540)	-
Rating changes	**(315)**	(362)	(658)
Rate differences	**2,433**	(2,482)	(801)
Entry into/exit from credit default	**494**	(210)	220
Net derivative transactions	**951**	(1,200)	(2,227)
Change in CVA	**267**	(233)	(765)
Offset of payroll tax in deferred taxes	**771**	1,979	-
Other	**(1,123)**	6,098	1,354
Closing balance	**277,344**	266,534	277,034

Changes in market risk-weighted assets

	For the year ended December 31		
	2017	2016	2015
	in NIS millions		
Opening balance	**4,788**	5,167	10,839
Interest rate risk - change in open positions	**(264)**	(605)	(3,175)
Foreign currency risk - change in open USD short positions	**128**	97	(1,154)
Equity risk - change in futures and options on stock indices	**(197)**	101	(1,155)
Option risk - change in forex options scenarios	**9**	28	(187)
Closing balance	**4,464**	4,788	5,167

Changes in operational risk-weighted assets

	For the year ended December 31		
	2017	2016	2015
	in NIS millions		
Opening balance	**20,843**	20,432	20,317
Change	**641**	411	115
Closing balance	**21,484**	20,843	20,432

The leverage ratio (Pillar 3)

Leverage ratio is defined as the measured regulatory capital divided by the measured exposure, with the ratio expressed as a percentage. The regulatory capital for the purpose of leverage ratio measurement is Tier 1 capital as defined in Proper Conduct of Banking Business Regulation No. 202, taking into account the transitional arrangements. A banking corporation's total exposure is the sum of the balance sheet exposures, exposure to derivatives, exposure to securities financing transactions and off-balance-sheet items. The leverage ratio complements the capital ratio and constitutes yet another constraint on the banking sector's leverage level.

The leverage ratio may be affected by changes in the Bank's regulatory capital. When calculating the leverage ratio, the following were taken into account, among others: the effect of the implementation of the efficiency plan and adjustments in respect of the implementation of the discount rate calculated over a moving average of the market yield for the eight quarters ended on the reporting date, in respect of certain actuarial liabilities, as outlined above.

Table 10 - Comparison of the balance sheet assets to the exposure measured for leverage ratio purposes (Pillar 3)

	December 31	
	2017	2016
	in NIS millions	
Total assets according to the consolidated financial statements	**450,838**	438,603
Adjustments for:		
Adjustments for entities in the field of banking, finance, insurance or trading consolidated for accounting purposes, but not under the consolidation scope for regulatory purposes	**-**	-
Trust assets recognized in the balance sheet in accordance with the Reporting to the Public Directives, but not included in the leverage ratio exposure measurement.	**-**	-
Derivative financial instruments[(a)]	**186**	(5,529)
Securities financing transactions	**-**	-
Off-balance sheet items	**45,524**	45,776
Other	**2,478**	2,534
Exposure for leverage ratio purposes	**499,026**	481,384

(a) The data as of December 31 2017, include the effects of the first-time application of directive, "Capital Requirements in respect of Exposures to Central Counterparties", which was implemented as of January 1 2017.

Table 11 - Leverage ratio - additional disclosure (Pillar 3)

Item	December 2017	2016
	in NIS millions	
Balance sheet exposures		
Balance sheet assets (excluding derivatives and securities financing transactions; including collateral)	**440,454**	426,996
Amounts in respect of assets deducted for the purpose of measuring Tier 1 capital	**(302)**	(319)
Total balance sheet exposures (excluding derivatives and transactions to finance securities)	**440,152**	426,677
Exposures for derivatives		
The replacement cost associated with all derivative transactions (e.g.: after the deduction of an eligible variable cash collateral)[(b)]	**1,401**	1,084
Additional amounts in respect of potential future exposure associated with all derivative transactions[(b)]	**10,274**	5,572
Gross-up of collateral provided in respect of derivatives, deducted from the balance-sheet assets in accordance with the Reporting to the Public Directives	**-**	-
Deductions of debtors' assets in respect of variable cash collateral provided in derivative transactions	**(1,916)**	(1,532)
Business exposures exempt from a central counterparty leg settled by the customer	**-**	-
Effective adjusted notional amount of written credit derivatives	**-**	-
Adjusted effective notional offsets and deduction of additions in respect of written credit derivatives	**-**	-
Total exposures for derivatives	**9,759**	5,125
Exposures for securities financing transactions	**-**	-
Gross assets for securities financing transactions (excluding recognition of off-sets), after adjustments for transactions accounted for as an accounting sale	**1,376**	1,609
Payable cash amounts and cash receivables offset from gross assets for securities financing transactions	**-**	-
Credit risk exposure of a central counterparty for securities financing assets	**-**	-
Exposures for securities financing transactions as agent	**2,215**	2,197
Total exposures for securities financing transactions	**3,591**	3,806
Other off-balance-sheet exposures		
Total off-balance-sheet exposure at a gross notional value	**125,966**	124,386
Of which: 0% conversion coefficient	**3,939**	3,411
10% conversion coefficient	**29,273**	27,618
20% conversion coefficient	**21,427**	21,362
50% conversion coefficient	**66,032**	66,506
100% conversion coefficient	**5,295**	5,489
(Adjustments for conversion to credit-equivalent amounts)	**(80,442)**	(78,610)
Total off-balance sheet exposure after conversion to credit value	**45,524**	45,776
Capital and total exposures		
Tier 1 capital[(a)]	**34,653**	32,586
Total exposures[(a)]	**499,026**	481,384
Leverage ratio		
Leverage ratio in accordance with Proper Conduct of Banking Business Directive No. 218	**6.94%**	6.77%

(a) These data include adjustments for the efficiency plans prescribed in the Supervisor of Banks' letter dated January 12 2016, Operational Efficiency of the Banking System in Israel. According to the said letter, the reliefs granted in respect of capital adequacy ratios and leverage ratio for the efficiency plans, which were approved by the Board of Directors in June 2016 and in July 2017, are being gradually withdrawn until June 30 2021 and June 30 2022, respectively. The effect on the leverage ratio of the relief for the efficiency plans was approximately 0.09% as at December 31 2017 (0.08% as at December 31 2016). For more information regarding the effect of the transitional provisions and adjustments for the efficiency plans, please see "Relief in respect of operational efficiency plans" as well as a table on this subject under "Capital Adequacy" below.

In addition, when calculating the leverage ratio, adjustments in respect of the implementation of the discount rate calculated over a moving average of the market yield for the eight quarters ended on the reporting date, in respect of certain actuarial liabilities, as outlined above were taken into account.

(b) The data as of December 31 2017, include the effects of the first-time application of directive, "Capital Requirements in respect of Exposures to Central Counterparties", which was implemented as of January 1 2017.

Risk management at Leumi

Managing risks and maximizing returns against them are fundamental to the Bank's business activity. The key risks managed by the Bank are financial ones: credit risks - which are integral to the Bank's core business, as well as market and liquidity risks. In addition, alongside these managed risks, the Bank's activities give rise to related risks, the management of which forms a crucial precondition to meeting the Group's immediate and long-term objectives. These risks include operational risks, such as technological and cyber risks, legal risks, regulatory risks, reputation risks, compliance risks, conduct risks and strategic risk.

The main objectives of risk management at Leumi are to maintain the Group's stability and support the achievement of its business goals. These objectives are achieved while meeting the predefined risk appetite, the policy and the limitations deriving therefrom, which form the boundaries for the business activity. This framework is managed subject to adequate control and reporting mechanisms.

The Bank continually upgrades its risk management infrastructure and analyzes the risk outlook, to enable informed decision-making.

The risk management methods and work procedures are regularly assessed and updated, taking into account the changes occurring in the business environment and the requirements of the Bank of Israel and other Israeli and foreign regulators.

The framework used for estimating and managing risk and decision-making includes the following:

a. The risk appetite - which outlines the boundaries of the business activity, both in the regular course of business and under stress scenarios, and which defines, inter alia, the policy and risk boundaries for each type of risk - is established.
b. Workflows are established for analyzing and managing risk at the individual transaction level as well as at the portfolio level.
c. Periodic risk assessment reports are prepared, addressing the changes in the Bank's environment. Estimates are made regarding potential losses and their implications for the Bank under scenarios of various severity levels
d. General and specific action plans for handling and mitigating risk are drawn.

Risk assessments are made at the Group-, activity- and individual transaction level, using several structured methodologies. Some are based on expert assessments in each area of activity while others are based on various types of statistical models. Changes in the Israeli and global risk environment and in the risk perception require Leumi to update its assessments and the methodologies it uses, which are constantly challenged by in-house parties and, from time to time, by external ones.

The risk management organizational structure

Leumi's risk management is based on three "lines of defense", as required by Proper Conduct of Banking Business Directive No. 310 - *Risk Management*.

1. First line of defense – the managements of the business lines, including supportive functions such as IT, bear full responsibility for managing the risks embodied in the products, operations, processes and systems under their purview, and for implementing an adequate control environment over their activities, through processes of identification, measurement, monitoring, control, mitigation and reporting

2. Second line of defense – The Risk Management Division is an independent function responsible for planning and developing a comprehensive risk management framework for the Bank. The Risk Management Division's main areas of responsibility conform to the requirements of the Proper Conduct of Banking Business Directive No. 310, including: responsibility for risk management at the Group and Bank levels; leading the drafting of Leumi's risk policy for all major risks; assisting the Board of Directors in determining the Bank's risk appetite; and leading the process of evaluating the Internal Capital Adequacy Assessment Process (ICAAP), including its various components. In addition, the Division is responsible for: granting letters of authority for credit activities; monitoring and control over the main risk appetite boundaries; establishing the framework for managing conduct risk; model development and validation; risk assessment and validation of borrowers' internal ratings in specific credit portfolios according to established thresholds; overall responsibility for the adequacy of the credit classifications and allowances and calculation of the collective allowance; real-time involvement in risk management for key and strategic projects; performance of independent analyses for strategic decision-making, approval processes of new products and forming an overall, up-to-date picture of the risk for decision-making purposes.

The second line of defense involves additional functions, such as: The Bank's Chief Legal Counsel - who is responsible for the management of legal risk and compliance risk, and the Accounting Division - which is responsible for financial reporting and SOX.

3. The third line of defense is the Internal Audit Division, which reports directly to the Board of Directors. The Internal Audit Division is responsible for conducting independent, objective reviews and for challenging controls, processes and risk management systems in the banking corporation. The audit is usually performed retrospectively on the first and second lines, ensuring implementation of the instructions of management and the Board of Directors

The Bank's Board of Directors is responsible, *inter alia*, for developing the overall risk strategy, including: the risk appetite; supervision of the Group's risk management framework; approval of the risk management policy for each material risk; overseeing and challenging the risk levels to which the Group and the Bank are exposed, while ensuring compliance with the risk appetite.

The Chief Risk Officer, who is a member of the Bank's management and heads the Risk Management Division, is responsible for managing the Group's and Bank's main risks.

On April 1 2017, Ms. Bosmat Ben Zvi was appointed Chief Risk Officer, in lieu of Ms. Hilla Eran-Zick.

Reporting to the Chief Risk Officer are the managers of the following units – Credit Risk Unit, Operational Risk Unit, Total Return Risk Unit, and the Credit Risk Unit Manager, who is responsible for credit risk at the individual transaction level. A chief risk officer is appointed for each Israeli and foreign subsidiary, reporting to the subsidiary CEO and indirectly (dotted line) to the Group's Chief Risk Officer.

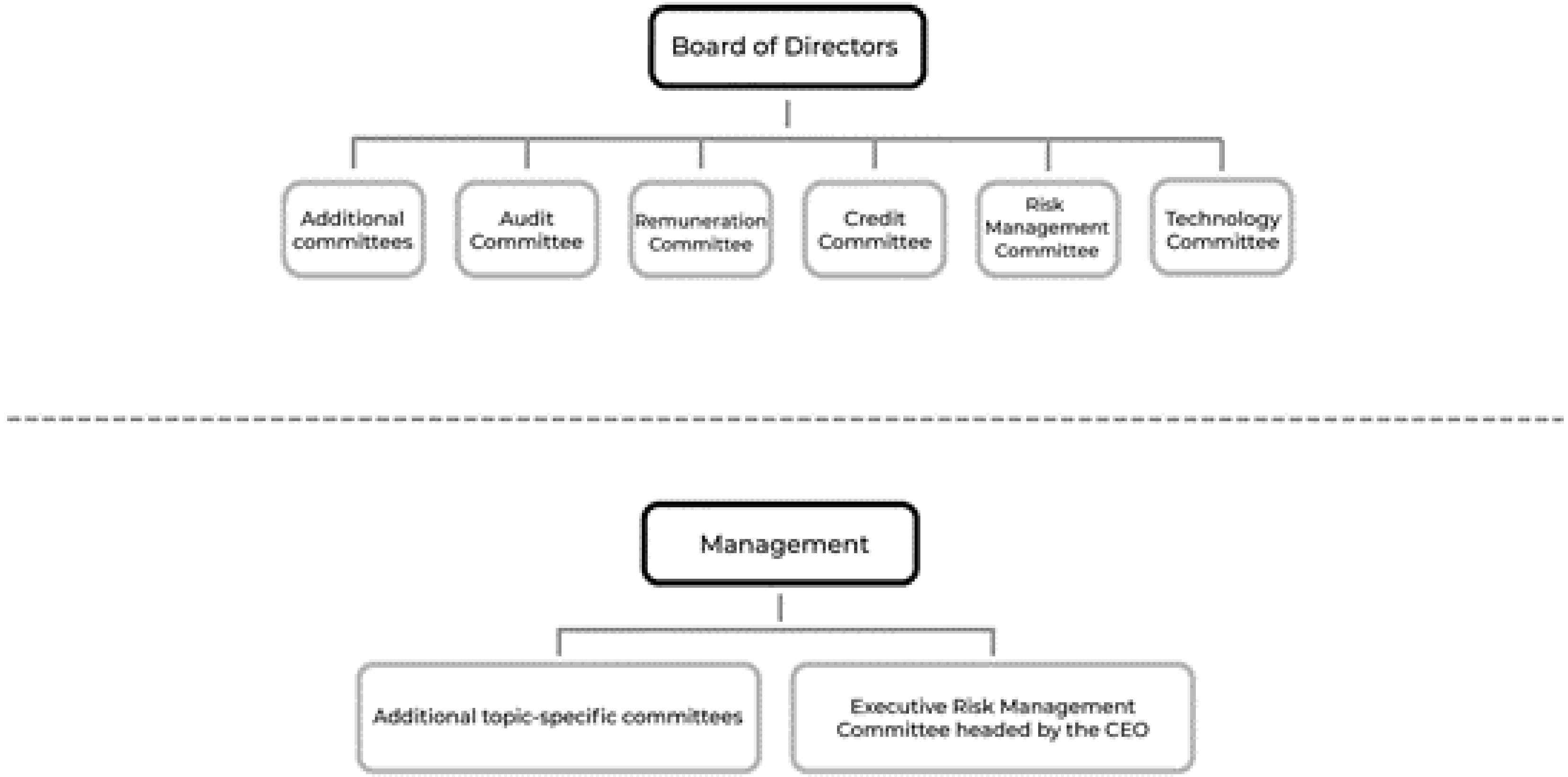
Risk management command and control is conducted by the committees responsible for managing the various risks, as follows:

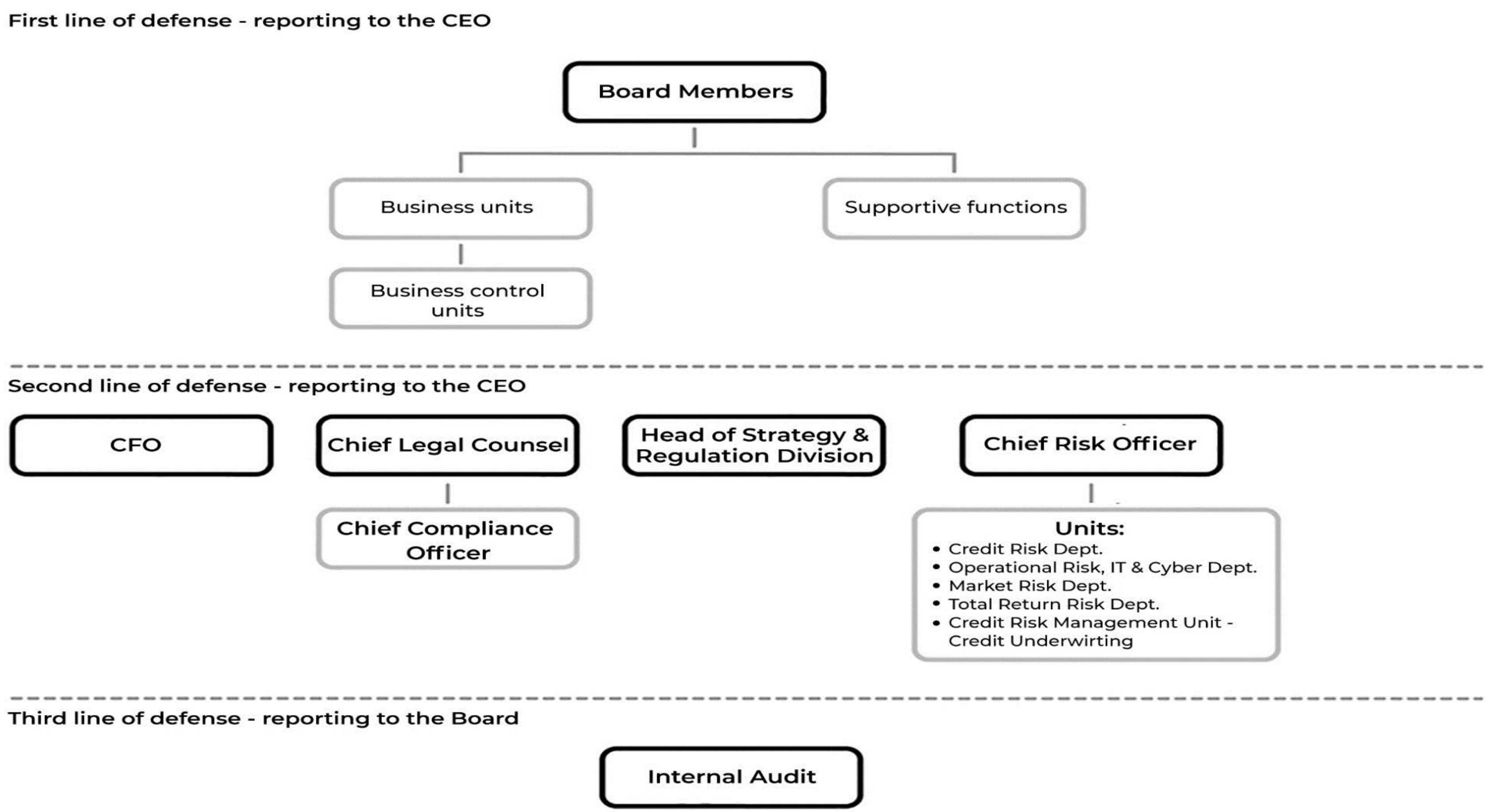
- The Board of Directors' Risk Management Committee.
- The Executive Risk Committee, which is headed by the President and CEO and whose members include all of members of management.
- Various risk management committees by topic, headed by the Chief Risk Officer, with the participation of the relevant business entities:
  - Executive Credit Risk Management Committee.
  - Executive Market Risk Management Committee.
  - Executive Operational Risk Management Committee.
  - Executive Foreign Subsidiaries Risk Management Committee.
  - Total Return Risk Committee.
  - Steering Committee for Credit Model Management.
- Executive Compliance Risk Management Committee headed by the Chief Compliance Officer.
- Committee for Implementation of Cross-Border Banking, headed by the Chief Legal Counsel.
- Disclosure Committee on the effectiveness of disclosure controls and procedures for the financial statements and changes in the internal control over financial reporting – SOX, headed by the President and CEO and whose members include all of members of management.

The various committees discuss aspects of the various risk exposures, direct the development of policy papers; examine the risk profile and prescribe internal boundaries and control processes in accordance with the market conditions and the Bank's risk appetite.

The subsidiaries manage risk in accordance with the principles prescribed at the Group level, with their policy papers corresponding to the Group's policy and reflecting relevant changes, as needed. Risk appetite, boundaries and permissions are established for each risk area, with control systems in place and periodic management reports examining the boundaries against the actual situation; supervision is exercised by each subsidiary's Board of Directors.

Table 12 – The Bank's Risk Management Governance





* The compliance and enforcement array reports to the Legal Counsel Division. Due to the organizational changes and appointments made at the Bank, until the end of 2017, the compliance and enforcement array reported to Hanan Friedman, who served as the Bank's Chief Legal Counsel and currently heads the Strategy and Regulation Division; since the beginning of 2018, the array reports to the

The risk management culture and its implementation

The Leumi Group maintains an organizational culture based on robust risk management, which is key to effective risk management. The Risk Management Division is involved in, and leads, the Group's key processes, in order to ensure that risk management processes are incorporated into the business activity. The Group's strategy is implemented in accordance with the risk appetite approved by the Board of Directors, through the use of advanced processes and tools for managing diverse types of risk and preparing for regulatory requirements. In addition, one of the remuneration principles is based on meeting the return on capital target, in accordance with the Group's risk appetite. In addition, the Bank believes in, and conducts ongoing training, to both reinforce the professionalism of the personnel involved in the Group's risk management and assimilate the risk management culture and risk management principles in various business lines.

The key principles underlying the Bank's risk culture are as follows:

- Corporate governance comprising three lines of defense (the business lines, independent risk management and internal audit).
- The Group's risk appetite and policy for managing various risks are approved by the Board of Directors. In addition, cross-organizational processes are held, such as the ICAAP, stress scenarios and integrating risk management into the Bank's work plan. The business activity and risk management and controls are organized effectively in order to minimize conflict of interest among the employees and Group-level units. The employees' professional level corresponds to the complexity of their functions and the risks they manage.
- Comprehensive differential risk management - Managing all material risks and their interfaces, while looking for correlations between various risks and emphasizing both the micro (the transaction/project) and macro levels, according to the risks' materiality.
- Introducing a new product approval process - A policy was defined for approving new products and supporting their assimilation, making significant changes in existing products or activities and entering new markets. The approval process involves examining the risks embodied in each new product and their effect on the risk profile, as well as whether the Bank has the required expertise and tools to identify, measure, monitor, control and report the new product's risks.
- The Bank's activity is managed pursuant to the principles of its Code of Ethics, which reflect the Bank's core values.

The Group's risk appetite

The Group's risk appetite outlines the boundaries for its business activity, both on an ongoing basis and under stress scenarios. The risk appetite is adjusted to Leumi's strategy and to the boundaries of its current and future business focal points. The risk appetite addresses Leumi's risk identification, measurement, control, management and mitigation practices, which have direct impact on the Group's residual risk profile. The risk appetite boundaries are re-examined each year and approved at the Board level as part of the ICAAP process. In December 2017, the Group's risk appetite was re-approved as part of the ICAAP paper.

The risk appetite paper constitutes a reference point for all risk-specific policy papers, which outline additional risk boundaries and risk management guidelines.

The Group's risk appetite statement covers the scope and types of aggregate risk the Bank is willing to take in order to achieve its business goals. Quantitative and qualitative measures were set, based on forward-looking assumptions which reflect the Group's aggregate risk appetite statements.

When determining its risk appetite, the Group continuously calculates its risk capacity - i.e., the maximum level of risk it is willing to take without breaching the capital, leverage, liquidity and commitment restrictions, as well as other regulatory restrictions, taking into account the perspectives of its shareholders and customers. The risk capacity is examined, *inter alia*, using sensitivity testing and stress scenarios

During Q1 2017, Bank Leumi implemented a global stress scenario for 2016 and 2017, prepared in accordance with the directives and requirements of the Bank of Israel.

The Leumi Group also implements a set of internal stress tests, updated on a regular basis, with the aim of assessing key risk focal points, taking into account various developments in the Bank's environment, such as changes in the business environment, regulatory requirements, etc. The Leumi Group's scenario set includes, inter alia: a global systemic scenario, a local systemic scenario, and a variety of topic-focused scenarios.

The impact of the most severe stress tests is also examined with respect to the Group's capital planning, in order to ensure the Group's compliance with all of the regulatory and internal restrictions set in respect of the realization of the various scenarios.

For more information, please see under "Exposure to Risk and Methods of Risk Management" in the Board of Directors and Management Report.

Risk profile - Defining risk factors' severity

Leumi's risk profile is examined on a quarterly basis, as part of the exposure report approved by the Board of Directors each quarter. The risk profile is examined, inter alia, by using a methodology for classifying the severity level of exposures to different risks. The methodology is based on quantifying the effect of various scenarios being realized on the Group's capital, i.e. its stability, and includes "expert assessments" by relevant functions in the Bank. In cases where a specific quantitative scenario does not adequately express the severity of a risk factor, greater weight will be given to a qualitative estimate.

For more information, please see under "Exposure to Risk and Methods of Risk Management" in the Report of the Board of Directors and Management.

Credit risk

Credit provision is a core activity of the Bank and the Group, which is conducted in a decentralized manner by various business lines.

Credit risk is the Bank's risk of loss as a result of the possibility that a counterparty fails to meet its agreed commitments towards the banking corporation.

Activities which increase credit risk include balance sheet credit risk and off-balance sheet credit risk, including: loans to the public, loans to banks, loans to governments, deposits with banks, investments in debentures, capital holdings, transactions in derivatives, guarantees, unutilized commitments to extend credit and unutilized credit lines.

The Bank applies a comprehensive risk management policy in line with the requirements of Proper Conduct of Banking Business Directive No. 311 and Proper Conduct of Banking Business Directive No. 314, including the accountability of management and the Board of Directors. In addition, the Bank is meticulous about managing risk in compliance with further guidelines and requirements included in the Banking Supervision Department's directives, implementing corporate governance which includes three "lines of defense".

Organizational structure and responsibility for credit risk management

First line of defense - The business lines

The Bank's credit risk is associated with several main business lines, according to their respective specializations. These business lines are responsible for taking the risk while analyzing, understanding and monitoring it throughout the life of a transaction. The business lines operate in an adequate risk environment, for which the following processes have been defined: credit underwriting, management and operation. The credit approval process is carried out pursuant to the Bank's credit policy and in line with a predefined hierarchical structure, including the involvement of the Credit Risk Management unit in the Risk Management Division (for more information, please see below).

In the first line of defense, control actions form an integral part of the risk management process. Within this line of defense, each of the business divisions includes a specialized unit which is responsible for operative and/or control aspects, as needed.

As such, the first line of defense includes units responsible for borrowers with repayment difficulties - either retail customers (Problem Debt Units, which report to the Banking Division) or mid-size companies and corporations (Special Credit Department), in accordance with Proper Conduct of Banking Business Directive No. 450.

Second line of defense - The Risk Management Division

The Risk Management Division includes two units responsible for handling credit risk, according to their respective purviews:

a. The Credit Risk Management Department (CRM)

The Credit Risk Management Department coordinates the entire range of second line defense activities and responsibilities associated with credit risk management at the transaction and individual customer levels, including: providing an in-depth and independent opinion on loan applications submitted by the business units; conducting independent validation of the borrower's internal risk rating; and a periodic sensitivity analysis of certain borrowers, in cooperation with the business units. This includes a vote on the main risks embodied in granting the loans and providing recommendations for continued handling of the customer, including with regard to classification and provisions.

The CRM units handle borrowers with credit of NIS 25 million and over in the Commercial, Business and Real Estate Department. In addition, the CRM units - in cooperation with the Credit Risk Unit (see Section B), and the Business-Commercial Division's management - establish methodologies and criteria for providing credit to specific sectors or market segments.

b. Credit Risk Management Department

While the activity of the CRM units focuses on analyzing individual borrowers and credit provision, the CRM Department is responsible for the management, control and analysis of credit risk at the aggregate level, i.e. - at the segment and total credit portfolio levels.

The Department's purview includes: directing the development of the Bank's credit and credit risk policy paper to be approved by management and the Board of Directors; establishing the internal boundaries at the portfolio level and continuous monitoring of compliance therewith; presenting the risk picture while analyzing the trends and changes over time (both at the overall portfolio level and by segment and business line); independently evaluating the management and control processes in the first line units; overall responsibility for validating internal credit ratings; responsibility for issuing recommendations for letters of authority to approve and update credit transactions; developing methodologies; executing and analyzing credit stress scenarios, and more. The CRM Department is also responsible for independent validation of classification and provision decisions regarding individual borrowers with credits ranging from NIS 5 million to NIS 25 million (as stated above, the CRM units validates decisions regarding customers with credit lines of NIS 25 million and over).

Third line of defense - Internal Audit

The Internal Audit Division conducts a retrospective independent review and challenging of the controls, processes and risk management systems in the banking corporation.

Corporate governance

The Bank is meticulous in maintaining adequate corporate governance in credit risk management processes. In addition to adhering to a clear, predefined hierarchy of credit approval at the individual transaction level, cross-organizational aspects of credit risk management are discussed by several key committees:

- Board of Directors' Risk Management Committee - each quarter, the committee discusses the Risk Management Division's risk paper, which includes credit risk exposures, and an overview of compliance with the boundaries at the Group and Bank levels.
- In addition, each year, the credit risk management policy - including the main internal boundaries - is discussed and approved by the committee, and the committee's recommendations are brought to the approval of the Board of Directors' plenum.
- Board of Directors' Credit Committee - each quarter, the committee holds a discussion dedicated to the credit section of the Risk Management Division's risk management paper. The discussion covers exposures to credit risks and trends in the main risk centers and includes an update on compliance with the boundaries at the Group and Bank levels, taking into account any material changes in the business and/or regulatory environment. The committee hears and discusses periodic reports on specific segments of the credit portfolio as well as the approval of specific and highly material credit applications.

- Executive Credit Risk Management Committee headed by the Chief Risk Officer - discusses all aspects pertaining to: credit policy; internal boundaries; key financing methodologies and procedures; monitoring of the risks and trends in the credit portfolio; and formulates recommendations on matters requiring approval by the Board of Directors.
- Steering Committee for Credit Model Management headed by the Chief Risk Officer - discusses all matters pertaining to the integrity of the Leumi Group's credit risk models, in compliance with the relevant regulations.

The Bank's credit policy

A group-level credit policy and credit risk paper is a prime expression of the Bank's credit risk strategy, outlining the framework and overarching principles for the policy papers of the Bank and each of the Group's subsidiaries in Israel and abroad. The paper also includes the credit boundaries, which are defined and managed at the group level.

The guiding principles of the Bank's credit policy are as follows:

- Focusing the exposures on activities for which the Bank has the expertise needed to estimate and manage the risks embodied therein. When entering a new area of activity, the Bank operates in accordance with a general "new product" policy approved by the Board of Directors.
- Taking proactive business actions for various types of credit for risk diversification purposes.
- The segmentation principle: Customers are assigned to business lines according to their turnovers and total outstanding debt, as well as the level of complexity and specialization required for a specific type of credit transaction.
- Taking a comprehensive view, and conducting analysis, of the customer's needs, the business and financial environment in which he/it operates, while maintaining the rules of fairness, disclosure and transparency involved in the credit activity.
- Any function in the Bank which gives rise to credit risk exposure must be aware of the risks involved in his/its purview and assume responsibility for their ongoing management. This includes awareness and management of compliance risk that may be associated with transactions (such as credit, passive or current ones).
- Ongoing and periodic monitoring of credit exposures in order to identify weaknesses as early as possible and to prepare accordingly.
- Quantitative assessment of credit risk, while assigning each customer an internal risk rating. To achieve this objective, the Bank has models and automated systems in place to support the process of assessing a borrower's risk level and estimating the expected loss therefrom.
- Distinguishing between three types of activities:
  - Low-risk activities or segments to which the Bank would like to provide credit and grow in.
  - Medium-risk activities or segments, where credit provision is decided on a case-by-case basis.
  - High-risk activities or segments to which the Bank tends to avoid increasing its exposure.
- An outline of industry sector categories by risk level. This outline is updated on an ongoing basis in accordance with periodic analyses of the various industry sectors and their segments, in accordance with the risks and prospects embodied in each sector. The industry outline serves as yet another tool in making individual credit granting decisions.
- Setting, managing and monitoring internal quantitative boundaries: The Bank also monitors borrowers' risk rating distribution, under various cross-sections.
- The Bank strives to increase customer managers' alertness and general awareness of possible adverse implications of environmental issues on projects it provides credit to. The Bank works to identify sensitive industries and integrate this exposure component when making credit decisions.
- Underwriting considerations include, among other things:
  - Characteristics a borrower is required to have for credit approval purposes: evaluation of repayment capacity; credit rating; business experience; financial data and various prerequisites for credit provision (e.g., financing rate, maximum exposure and acceptable collateral).
  - The credit authority hierarchy defines who is authorized to approve exceptional credit applications, including the pricing component. There is also a hierarchy of powers for pricing decisions.
  - Guidelines for setting repayment schedules according with the purpose and nature of the loan and in accordance with the borrower's repayment capacity, expected source of payments, the collateral's life, etc.

It should be noted that there were no material changes in the Bank's credit policy in 2017.

The subsidiaries' credit policies

Each of the Bank's subsidiaries - including its foreign offices - has a credit policy paper based on the principles set forth in the Group policy paper and approved by the subsidiary's Board. The subsidiaries' policy papers and their conformance to the Group's policy are also reviewed by the Risk Management Division in Israel. Each quarter, a summary description of the subsidiaries' credit activity and the main characteristics of the credit portfolio are presented to the Bank's Board of Directors in Israel.

In the foreign offices, as in Israel, the credit policies are based on risk diversification and setting boundaries on exposure to various industries and operational segments. However, the level of concentration in the foreign offices is greater than in Israel, due to their relatively small size and the need to focus on and specialize in specific niches. Each foreign office is authorized to grant credit in various scopes and borrowers undergo an internal rating process. In addition, each subsidiary's risk officer is responsible for credit risk management functions that regularly perform independent assessments and monitoring of the risk level of the Bank's customers.

Credit risk management tools

To manage credit risk, quantitative models are used to internally rate borrowers' risk and evaluate and monitor risk at the portfolio level, with the internal rating of borrowers forming a key layer in the decision-making and credit-pricing processes and in monitoring its quality over time.

The Bank uses two main tools to assign internal ratings to customers:

A rating system for retail customers, based on the characteristics of the customer's activity in the account over time.

A borrower rating system designed for business-commercial borrowers, based on structured expert questionnaires.

The models used to perform the ratings in said systems are validated and monitored on a regular basis.

Delinquent and impaired loans

The Bank implements the Reporting to the Public Directives on impaired debts, credit risk, and allowance for credit losses.

The treatment of these directives is regulated by individual procedures and guidelines for the relevant parties. The following paragraphs outline only certain key aspects in this area with respect to the classification of debts and determining credit losses allowances.

Impaired debt

Balance sheet debt shall be classified as impaired under the following conditions:

- A customer has a negative, non-temporary debt service capacity from all sources.
- A debt was examined individually and found to be delinquent for least 90 days, unless it is adequately secured and in collection proceedings.
- According to a business analysis of recent events, there is a low probability that the debt will be repaid according to the loan agreement terms and conditions.
- The debt was restructured as problem debt and, as a result, will not be repaid under the original terms and conditions of the loan agreement.

An off-balance-sheet credit exposure will be classified as impaired if the liability for this debt is expected to materialize and the resulting balance sheet debt should be classified as impaired.

Delinquent debt

The delinquency status of a debt is determined according to the contractual repayment terms and conditions. Following are three possible delinquency situations:

1. Delinquency due to failure to repay a loan according to the contractual repayment terms and conditions.
2. An overdrawn current account.
3. Low turnover - as long as the account has not been credited with amounts needed to cover the debt within the defined period, even if the debt is within the credit line.

Rules for classifying debt according to the delinquency period:

- A debt examined individually and found to be delinquent for least 90 days shall be classified as impaired, unless it is adequately secured and in collection proceedings.

- The debt in question shall be classified according to the following rules:
  - Debt under special supervision - debt automatically flagged under certain negative criteria.
  - Substandard debt - debt that is delinquent for 90-149 days.
  - Impaired debt - debt delinquent for at least 150 days. In this case, there will be full allowance for the debt and it will be written off.

Allowance for credit losses

The Risk Management Division is responsible for setting appropriate classifications and allowances for credit losses.

Individual allowance

An allowance for credit losses is made for a debt classified as impaired and examined individually. The allowance is assessed according to the difference between the recorded outstanding balance of the debt and the present value of the future cash flows expected to service the debt from the customer's activity and the realization of the collateral and other assets, discounted at the effective interest rate of the debt. Each quarter, the allowance for the debts is examined, including, inter alia, in light of significant changes in the amounts or timing of expected cash flows due to be received in accordance with the updated estimates. For debts the repayment of which relies on collateral (collateral-contingent debts) and there are no other available and reliable sources of repayment, the allowance is determined based on the fair value of the collateral less disposal costs of and after triggering buffers in respect of the collateral's value so that it will be possible to realize the collateral and have the debt repaid therefrom.

The greater the uncertainty in respect of the cash flows, and the lower the level of confidence that the forecasts materialize, the more likely buffers will be used to reduce cash flows, thus providing reasonable confidence that the allowance is adequate.

Collective allowance

The collective allowance reflects an estimate of credit losses based on past losses in respect of debts with similar characteristics, with adjustments made for current risk assessments. This allowance is applied in respect of debts examined individually and found to be unimpaired.
The method of determining a collective credit loss allowance is in accordance with the requirements of the Reporting to the Public Directives, the main points of which are as follows:

- Loans to the public are split according to industry. For each industry, two rates of collective allowance are determined: one in respect of non-problem debts, and the other - higher - for problem debts (debt classified as "under special supervision" or "substandard"). These rates are based on past losses (the average of the net write-offs in the current year and in the previous full calendar years, since 2011).
- The rate of past losses is added to the "quality adjustment factor" - an additional coefficient for environmental factors relevant to the prospects of collecting the credit ("quality adjustments"), such as: industry-specific characteristics; the local economy's characteristics; and the composition and quality of the loan portfolio. To calculate the "quality adjustment factor", the Bank applies an internal formula which takes into account a wide range of indicators.

The allowance is calculated and made in respect of all the debts - both balance sheet credit and off-balance sheet credit instruments - with the off-balance sheet credit multiplied by a conversion coefficient according to the type of instrument and in accordance with the directives of the Supervisor of Banks.

Updates of Banking Supervision Department's directives on classifying problem debts according to the primary source of repayment

On February 20 2017, an update was published by the Banking Supervision Department to a Q&A file entitled, *Questions and Answers and Examples of Implementation of Public Reporting. Directives on Impaired Debts, Credit Risk, and the Allowance for Credit Losses*. The update mainly deals with the classification of debt, definition of impaired debt and measuring individual allowances for credit losses. Determining the appropriate classification of debt, until the occurrence of a failure or when its likelihood becomes highly probable, is based on the debtor's repayment capacity, i.e.: the expected robustness of the primary source of repayment, notwithstanding the support of secondary and tertiary sources of repayment (such as: collateral, a guarantor's support, refinancing by a third party).

The Bank has been applying these changes as of July 1 2017, as required by the Bank of Israel.

Table 13 - Changes in the balance of allowance for credit losses

	For the year ended December 31 2017

	Allowance for credit losses					
	Loans to the public					
	Commercial	Housing	Individuals - other	Total	Banks and governments	Total
	in NIS millions					
Balance of allowance for credit losses as at the beginning of the year	**2,685**	**473**	**823**	**3,981**	**1**	**3,982**
Other changes in allowance for credit losses	**-**	**-**	**-**	**-**	**-**	**-**
Expenses (income) for credit losses	**(5)**	**(13)**	**188**	**170**	**2**	**172**
Write-offs	**(835)**	**(9)**	**(581)**	**(1,425)**	**-**	**(1,425)**
Collection of debts written off in previous years	**678**	**-**	**364**	**1,042**	**-**	**1,042**
Net write-offs	**(157)**	**(9)**	**(217)**	**(383)**	**-**	**(383)**
Adjustments from translation of financial	**(19)**	**(1)**	**-**	**(20)**	**-**	**(20)**
Balance of allowance for credit losses as at year end[1]	**2,504**	**450**	**794**	**3,748**	**3**	**3,751**
Of which: For off-balance sheet credit instruments[1]	**448**	**-**	**36**	**484**	**-**	**484**

	For the year ended December 31 2016					
	Allowance for credit losses					
	Loans to the public					
	Commercial	Housing	Individuals - other	Total	Banks and governments	Total
	in NIS millions					
Balance of allowance for credit losses as at the beginning of the year	2,981	513	659	4,153	3	4,156
Other changes in allowance for credit losses	-	-	-	-	-	-
Expenses for credit losses	(571)	(9)	457	(123)	(2)	(125)
Write-offs	(566)	(31)	(693)	(1,290)	-	(1,290)
Collection of debts written off in previous years	843	-	400	1,243	-	1,243
Net write-offs	277	(31)	(293)	(47)	-	(47)
Adjustments from translation of financial statements	(2)	-	-	(2)	-	(2)
Balance of allowance for credit losses as at year end[1]	2,685	473	823	3,981	1	3,982
Of which: For off-balance sheet credit instruments[1]	452	-	36	488	-	488

	For the year ended December 31 2015					
	Allowance for credit losses					
	Loans to the public					
	Commercial	Housing	Individuals - other	Total	Banks and governments	Total
	in NIS millions					
Balance of allowance for credit losses as at the beginning of the year	3,365	513	604	4,482	4	4,486

Other changes in allowance for credit losses	-	-	-	-	-	-
Expenses for credit losses	(123)	14	309	200	(1)	199
Write-offs	(676)	(12)	(614)	(1,302)	-	(1,302)
Collection of debts written off in previous years	410	-	361	771	-	771
Net write-offs	(266)	(12)	(253)	(531)	-	(531)
Adjustments from translation of financial	5	(2)	(1)	2	-	2
Balance of allowance for credit losses as at year end[1]	2,981	513	659	4,153	3	4,156
Of which: For off-balance sheet credit instruments[1]	449	-	33	482	-	482

Credit concentration

Concentration risk is defined as a single exposure or group of exposures having a common attribute and the potential to cause significant losses. Concentration risk is mainly managed by setting boundaries and monitoring and controlling compliance therewith. The concentration aspect is also expressed in the credit's pricing, which reflects the risk.

The sources of concentration relevant to the Bank's credit portfolio are: industries, single borrowers and groups of borrowers.

The concentration risk is managed by ensuring compliance with all regulatory restrictions, as well as by defining and regularly monitoring compliance with all internal restrictions (which are more stringent than regulatory ones).

The Banking Supervision Department's directives regarding credit risk analysis of the car industry

On July 9 2017, the Banking Supervision Department published guidelines on credit risk analysis for the car industry. Pursuant to the guidelines, banking corporations and credit card companies are required to perform credit risk analysis of the "vehicle trade" industry and consumer car loans. The risk analysis will be performed using various scenarios which may affect the industry, and according to the results of this analysis - banks and credit card companies will be required to assess whether to update their credit policies, risk appetites, rules and restrictions for granting car loans as well as the need to tighten controls for significant existing borrowers and consumer car loans.

The Bank analyzed the relevant segments according to the directives of the Banking Supervision Department, and following a discussion held by the Board of Directors, several updates to the credit policy were approved.

Updates of the directives of the Banking Supervision Department on industry indebtedness

On July 10 2017, a circular was published, revising Proper Conduct of Banking Business Directive No. 315, *Additional Allowance for Doubtful Debts*. The directive was revised to minimize the adverse effect of industry concentration on the credit portfolio's quality, and as part of the policy of regulatory reliefs and process streamlining. The newly revised directive addresses the following issues, among others:

- An industry threshold was determined, according to which the indebtedness of a specific sector will not exceed 20% of all public debts to a banking corporation, or 22% in certain cases. The threshold will serve as the maximum upper indebtedness limit per industry. In addition, the directive was renamed, *Industry Indebtedness Limitation.*
- The additional allowance and general allowance mechanism was revoked.

In light of the revocation of the foregoing additional allowance mechanism, at the same time as the revised Proper Conduct of Banking Business Directive no. 315 was published, Proper Conduct of Banking Business Directive No. 314, *Adequate Assessment of Credit Risks and Adequate Measurement of Debts* was revised. According to the revised directive, when determining the allowance for credit losses, the banking corporation must take into account, inter alia, credit in respect of which there are no up-to-date financial statements.

These changes entered into effect on January 1 2018. The Bank examined the revisions to the directive and complies with the restrictions pursuant to the revised directive.

Table 14 - Distribution of exposure by main industries

	December 31 2017

	Total credit risk[(a)]	Debts[(b)]		Problem debts[(d)]			Credit losses[(c)]		
	Total	Total	Non-problem	Problem, unimpaired	Impaired	Delinquent debt	Expenses (income) for credit losses	Net write-offs	Balance of allowance for credit losses
	in NIS millions								
In respect of borrower activity in Israel Public-commercial									
Construction & real estate - construction[(e)]	**49,689**	**18,936**	**18,489**	**210**	**237**	**77**	**72**	**45**	**(350)**
Construction & real estate - real estate development	**27,700**	**24,444**	**23,833**	**120**	**491**	**57**	**(302)**	**(255)**	**(394)**
Financial services	**21,721**	**11,189**	**11,181**	**5**	**3**	**9**	**(76)**	**(56)**	**(188)**
Commercial-public	**93,340**	**70,580**	**67,754**	**1,477**	**1,349**	**244**	**236**	**310**	**(1,205)**
Commercial - total[(f)]	**192,450**	**125,149**	**121,257**	**1,812**	**2,080**	**387**	**(70)**	**44**	**(2,137)**
Individuals - housing loans	**79,034**	**77,448**	**76,726**	**722**	**-**	**1,238**	**(10)**	**8**	**(443)**
Individuals - other	**68,649**	**38,395**	**37,745**	**511**	**139**	**312**	**189**	**217**	**(790)**
Total credit to the public - activity in Israel	**340,133**	**240,992**	**235,728**	**3,045**	**2,219**	**1,937**	**109**	**269**	**(3,370)**
Banks in Israel	**3,921**	**1,650**	**1,650**	**-**	**-**	**-**	**2**	**-**	**(3)**
Government of Israel	**41,161**	**129**	**129**	**-**	**-**	**-**	**-**	**-**	**-**
Total activity in Israel	**385,215**	**242,771**	**237,507**	**3,045**	**2,219**	**1,937**	**111**	**269**	**(3,373)**
Total foreign activity	**100,256**	**41,024**	**39,558**	**767**	**699**	**20**	**61**	**114**	**(378)**
Total	**485,471**	**283,795**	**277,065**	**3,812**	**2,918**	**1,957**	**172**	**383**	**(3,751)**

(a) Balance-sheet credit risk and off-balance-sheet credit risk, including for derivatives. Including debt, debentures, securities borrowed or purchased under agreements to resell, assets in respect of derivatives and credit risk embodied in off-balance-sheet financial instruments, as calculated for the purpose of per-borrower credit limitations in the amounts of NIS 283,795, 73,065, 1,161, 9,580 and 117,870 million, respectively .

(b) Loans to the public, loans to governments, deposits with banks and other debts, excluding debentures and securities borrowed or purchased under agreements to resell.

(c) Including for off-balance-sheet credit instruments (presented in the balance sheet under "Other liabilities").

(d) Off-balance sheet credit risk that is impaired, substandard or under special supervision, including housing loans for which there is allowance according to the delinquency period and housing loans for which there is no allowance based on the delinquency period which are in arrears of 90 days or more.

(e) Including housing loans extended to certain purchasing groups currently in the process of construction.

(f) The balance of outstanding commercial debts includes outstanding housing loans in the amount of NIS 1,066 million extended to purchasing groups currently in the process of construction.

For more information regarding exposure to problem credit and changes in the allowance for credit losses, please see the Report of the Board of Directors and Management and Notes 13 and 31 to the Financial Statements. For more information on credit exposures by industry, please see the Report of the Board of Directors and Management.

	December 31 2016(*)								
	Total credit risk(a)	Debts(b)		Problem debts(d)			Credit losses(c)		
	Total	Total	Non-problem	Problem, unimpaired	Impaired	Delinquent debt	Expenses (income) for credit losses	Net write-offs	Balance of allowance for credit losses
	in NIS millions								
In respect of borrower activity in Israel Public-commercial									
Construction & real estate - construction(e)	45,662	15,576	15,037	275	264	77	(7)	26	(327)
Construction & real estate - real estate development	26,440	23,878	22,881	360	637	47	(303)	(65)	(426)
Financial services	19,520	10,854	10,390	5	459	4	(82)	(23)	(218)
Commercial-public	90,189	68,414	65,119	1,745	1,550	209	(151)	(263)	(1,279)
Commercial - total(f)	181,811	118,722	113,427	2,385	2,910	337	(543)	(325)	(2,250)
Individuals - housing loans	80,570	78,645	77,926	719	-	1,249	(10)	25	(462)
Individuals - other	67,691	38,141	37,502	531	108	374	458	293	(818)
Total credit to the public - activity in Israel	330,072	235,508	228,855	3,635	3,018	1,960	(95)	(7)	(3,530)
Banks in Israel	4,370	1,742	1,742	-	-	-	(2)	-	(1)
Government of Israel	41,992	206	206	-	-	-	-	-	-
Total activity in Israel	376,434	237,456	230,803	3,635	3,018	1,960	(97)	(7)	(3,531)
Total foreign activity	98,931	40,032	38,986	411	635	137	(28)	54	(451)
Total	475,365	277,488	269,789	4,046	3,653	2,097	(125)	47	(3,982)

(a) Balance-sheet credit risk and off-balance-sheet credit risk, including for derivatives. Including debt, debentures, securities borrowed or purchased under agreements to resell, assets in respect of derivatives and credit risk embodied in off-balance-sheet financial instruments, as calculated for the purpose of per-borrower credit limitations in the amounts of NIS 277,488, 75,259, 1,284, 10,659 and 110,675 million, respectively .
(b) Loans to the public, loans to governments, deposits with banks and other debts, excluding debentures and securities borrowed or purchased under agreements to resell.
(c) Including for off-balance-sheet credit instruments (presented in the balance sheet under “Other liabilities").
(d) Off-balance sheet credit risk that is impaired, substandard or under special supervision, including housing loans for which there is allowance according to the delinquency period and housing loans for which there is no allowance based on the delinquency period which are in arrears of 90 days or more.
(e) Including housing loans extended to certain purchasing groups currently in the process of construction.
(f) The balance of outstanding commercial debts includes outstanding housing loans in the amount of NIS 909 million extended to purchasing groups currently in the process of construction.
* Restated.

For more information regarding exposure to problem credit and changes in the allowance for credit losses, please see the Report of the Board of Directors and Management and Notes 13 and 31 to the Financial Statements.For more information on credit exposures by industry, please see the Report of the Board of Directors and Management.

Activity and risk boundaries in the construction and real estate industry

The real estate industry is the area of activity in which the Bank has the greatest exposure of all the business industries in the Israeli economy. As with other industries, the credit policy outlines methodologies and criteria for financing transactions in each of the real estate industry's segments.

Leumi's focus on real estate financing is reflected, inter alia, in the fact that a significant part of the Bank's activity is concentrated in a dedicated department specializing in serving customers in this area. The Construction and Real Estate Department finances some of the most extensive and/or complex transactions in this field, leveraging its credit officers' expertise and practical experience.

A significant portion of construction and infrastructure loans are extended under the construction loan model, which is characterized by periodic assessment and close monitoring of relevant criteria (such as: sales, construction progress, staying within budget, etc.). This is done by relying in part on certified outsourced construction supervisors.

The Bank closely monitors the real estate credit portfolio, while following macroeconomic trends and the development of the industry's risk characteristics.

The Bank also assesses the real estate industry risk under a central stress scenario, with credit losses broken down by sub-sectors and examined against the risk assessment and risk appetite.

The credit risk for the construction and real estate industry in Israel constitutes approximately 22.75% of the total credit risk in Israel.

According to the calculation rules set by the Bank of Israel for the purpose of determining an industry's concentration risk pursuant to Proper Conduct of Banking Business Directive No. 315, *Industry Indebtedness Limitation,* the industry's total indebtedness to the Bank is 19.03% of the total indebtedness in Israel.

On March 8 2016, an agreement was signed with international reinsurers with high global credit rating, for the purchase of an insurance policy for a portfolio of guarantees pursuant to the Sales (Apartments) Law and the portfolio of commitments to issue such guarantees. The policy insures the Bank against payment for the forfeiture of the guarantees, according to the terms and conditions of the policy. The purchase of the insurance policy enabled the Bank to reduce the capital set aside in respect of the credit risk arising from the issuance of the guarantees, while using the policy as a "credit risk mitigator". The insurance is for projects commencing by August 1 2018.

In addition to the regulatory limit and in order to effectively manage the internal credit risk mix, the Bank is careful to apply geographical diversification to the projects, according to demand and across the different sub-sectors.

As of December 31 2017, the Bank complies with the regulatory and internal restrictions, which are in line with the Bank's assessment of the risk embodied in the various sub-sectors.

Table 15 - Development of indebtedness for the construction and real estate industry

	December 31		Change from end of previous year	
	2017	2016		
	in NIS millions		in NIS millions	In %
Balance-sheet credit risk	**53,861**	49,368	4,493	9%
Guarantees for apartment buyers[(a)]	**8,082**	8,421	(339)	(4)%
Other off-balance-sheet credit risk[(a)]	**29,669**	28,035	1,634	6%
Total credit risk	**91,612**	85,824	5,788	7%

(a) In credit risk terms.

Housing loan portfolio risks

Economic developments in Israel in recent years (primarily a low interest environment and a sharp hike in housing prices) have led to a significant increase in housing credit provision.

The housing loan portfolio is monitored and the trends in its characteristics and risk centers analyzed on a regular basis, including monitoring of the distribution of credit by linkage base, interest rate, and down payment.

Table 16 - Development of total outstanding housing loans in Israel, net

	Outstanding loans portfolio	Change from end of previous year
	in NIS millions	in %
December 31 2015	80,616	8.5
December 31 2016	78,656	(2.4)
December 31 2017	**77,005**	**(2.1)**

2017 saw a decline in the volume of housing loans, due to a decrease in the number of loans being granted and the sharing of loan-granting with an institutional entity.

As part of its monitoring of risk centers in the housing loan portfolio, the Bank also monitors characteristics of new credit, including the new credit's distribution by financing rates (financing rate is the ratio of the total credit approved for the borrower - even if it has not yet been actually extended either in full or in part - out of the value of the mortgaged property during the approval of the credit line).

Table 17 - Development of new outstanding credit granted in Israel at a financing rate of over 60%

	2017	2016	2015
	Annual average		
Financing rate	In %[(a)]		
Over 60 to 70, inclusive	**18.1**	16.1	18.8
Over 70 to 80, inclusive	**16.2**	14.7	16.7
Over 80	**0.1**	0.1	1.1

(a) Out of the total new credit granted by the Bank.

For more information about this segment, please see under "Credit risk" in the Report of the Board of Directors and Management.

Credit risk in respect of loans to individuals (excluding housing loans)

Credit granted to individuals, whose repayment capacity is largely based on their household's earning capacity, is characterized by a very wide dispersion of borrowers and a variety of credit products (various types of loans, current accounts, credit cards) and to a lesser extent (on average) - credit per individual customer.

Individual customers' activity is almost entirely concentrated in the Banking Division.

To address the increase in credit granted to individuals and given the wide span of control required to manage it, and with the aim of implementing adequate corporate governance, several functions have been extended and enhanced, both in the Banking Division - which constitutes the first line of defense, and in the Risk Management Division - which constitutes the second line of defense.

The retail credit policy, formulated by the Risk Management Division in collaboration with the Banking Division, constitutes an important element in outlining the risk appetite and ongoing management of this domain. The following are some of the key principles of the Bank's consumer credit policy: assess each borrower's credit risk; base underwriting decisions on the borrower's debt service capacity, especially his income; create a well-defined, structured chain of command for authorizing credit; adhere to fair business conduct practices (integrity; transparency; match products to customers' needs; fair pricing; address customer complaints); match the credit to the customers' needs and capacity; and increase awareness of the compliance aspects that could arise from credit provision.

Due to the increased debt levels of Israeli households in recent years and the expectation that the trend will continue, the Bank extended and boosted its ongoing monitoring of its entire consumer credit portfolio, in addition to its adherence to strict underwriting processes and management and control at the individual borrower level.

For more information about this segment, please see under "Credit risk" in the Report of the Board of Directors and Management.

Geographic distribution

The credit portfolio's geographic distribution is designed to mitigate the risk that an economic, political or security crisis in the countries to which the borrower is exposed could harm his/its financial position and his capacity to meet his/its obligations.

As part of the information used to determine a corporate borrower's internal risk rating, aspects of geographic exposure are taken into account, in particular the location of cash flow sources and/or physical assets used by the borrower on an ongoing basis. Such information enables the Bank to obtain an overview of, and monitor, the exposure of all borrowers to various countries.

To date, the Bank's credit portfolio has no significant concentration in terms of exposure of corporate borrowers to any foreign country.

For more information about credit exposures to foreign countries, please see under "Credit risk" in the Report of the Board of Directors and Management.

Table 18 - Distribution of total credit risk by geography

	December 31 2017			
		Foreign countries		
	Israel	USA	UK	Other
	in NIS millions			
Loans To the public[(a)]	**244,749**	**17,267**	**5,216**	**720**
Securities[(b)]	**71,657**	**5,121**	**113**	**408**
Derivatives[(c)]	**9,525**	**34**	**14**	**-**
Other balance sheet exposure[(d)]	**91,813**	**1,956**	**1,949**	**296**
Off-balance sheet, excl. derivatives[(e)]	**92,156**	**6,201**	**2,003**	**174**
Total exposure to derivatives (balance sheet and off-balance sheet)[(f)]	**17,741**	**57**	**21**	**-**

	December 31 2016			
		Foreign countries		
	Israel	USA	UK	Other
	in NIS millions			
Loans To the public[(a)]	238,346	17,329	5,566	672
Securities[(b)]	70,694	5,927	120	459
Derivatives[(c)]	10,569	50	36	-
Other balance sheet exposure[(d)]	80,752	5,122	2,502	458
Off-balance sheet, excl. derivatives[(e)]	90,935	7,156	1,674	184
Total exposure to derivatives (balance sheet and off-balance sheet)[(f)]	16,097	72	45	-

(a) Balance-sheet credit risk that includes loans to the public less allowance for credit losses.
(b) Balance sheet balances of available-for-sale, held-for-trading and held-to-maturity securities, including shares and funds, excluding securities borrowed or bought under agreements to resell.
(c) Balance sheet balance of assets in respect of derivative instruments.
(d) Including cash and deposits with banks, credit to governments, investment in associates, buildings and equipment and other assets.
(e) Credit risk for off-balance sheet credit instruments as calculated for the purpose of per borrower credit limitations, excluding for derivatives.
(f) Total balance-sheet and off-balance-sheet credit risk for derivatives.

Breakdown of the portfolio by credit exposure type

Table 19 - Credit risk exposures by main type of exposure (Pillar 3) [a]

	December 31			
	2017		2016	
	Credit risk exposures, gross[b]	Average credit risk exposures, gross	Credit risk exposures, gross[b]	Average credit risk exposures, gross
	in NIS millions			
Type of credit exposure:				
Credit[c]	**348,371**	**337,647**	336,655	325,367
Debentures[d]	**69,785**	**70,424**	67,611	66,379
Other[e]	**18,046**	**17,560**	16,653	16,767
Guarantees and commitments on account of	**126,119**	**126,129**	124,542	128,233
Transactions in derivatives[f]	**13,892**	**13,569**	8,465	8,524
Total	**576,213**	**565,329**	553,926	545,270

(a) After deducting write-offs and before deducting credit loss allowances on an individual and collective basis.
(b) Before conversion of off-balance-sheet components to credit (e.g., taking into account unutilized credit lines), before credit risk mitigation through certain actions (for example, through guarantees) and after netting derivative transactions.
(c) Including loans to the public, loans to the government and deposits with central banks, and after deducting liabilities for transactions in derivatives subject to CSA agreements.
(d) Excluding the debentures in the marketable portfolio and excluding capital investments in financial institutions.
(e) Including cash, investments in financial institutions which have not been deducted from capital, tax prepayments, shares and other assets without a counterparty, such as: buildings and equipment.
(f) Positive fair value of derivatives, including an add-on that reflects the potential amount of the future exposure to credit in respect of the balance of the derivative instruments' par value and after netting derivative transactions. In addition, as of January 1 2017, changes have been made in the calculation of exposures to major counterparties. The effect of the application led to a NIS 3.5 billion increase in derivative exposures.

Table 20 - Credit risk exposures by counterparty and type of exposure (Pillar 3)[a]

	December 31 2017					
	Credit[c]	Debentures[d]	Other[e]	Guarantees and other commitments	Transactions in derivatives[f]	Total[b]
	in NIS millions					
Sovereign debts	**70,340**	**48,582**	**-**	**619**	**91**	**119,632**
Debts of public sector entities	**4,961**	**9,553**	**-**	**1,148**	**115**	**15,777**
Debts of banking corporations	**9,441**	**5,958**	**-**	**4,321**	**7,052**	**26,772**
Debts of securities issuers	**18**	**721**	**-**	**-**	**1,130**	**1,869**
Debts of corporations	**87,515**	**2,279**	**-**	**41,676**	**5,455**	**136,925**
Debt collateralized by commercial	**36,313**	**-**	**-**	**37,824**	**-**	**74,137**
Retail exposures to individuals	**44,116**	**-**	**-**	**30,974**	**41**	**75,131**
Loans to small businesses	**18,372**	**-**	**-**	**5,104**	**8**	**23,484**
Housing mortgages	**77,295**	**-**	**-**	**4,453**	**-**	**81,748**
Securitization	**-**	**2,692**	**-**	**-**	**-**	**2,692**
Other assets	**-**	**-**	**18,046**	**-**	**-**	**18,046**
Total for credit risk	**348,371**	**69,785**	**18,046**	**126,119**	**13,892**	**576,213**

	December 31 2016					
	Credit[c]	Debentures[d]	Other[e]	Guarantees and other commitments	Transactions in derivatives[f]	Total[b]
	in NIS millions					
Sovereign debts	67,437	48,146	-	743	24	116,350
Debts of public sector entities	4,679	9,007	-	764	140	14,590
Debts of banking corporations	5,981	4,687	-	4,927	3,652	19,247
Debts of securities issuers	-	462	-	-	659	1,121
Debts of corporations	86,160	2,274	-	43,343	3,961	135,738
Debt collateralized by commercial	33,001	-	-	35,551	-	68,552
Retail exposures to individuals	44,455	-	-	30,074	28	74,557
Loans to small businesses	16,473	-	-	4,857	1	21,331
Housing mortgages	78,469	-	-	4,283	-	82,752
Securitization	-	3,035	-	-	-	3,035
Other assets	-	-	16,653	-	-	16,653
Total for credit risk	336,655	67,611	16,653	124,542	8,465	553,926

(a) After deducting write-offs and before deducting credit loss allowances on an individual and collective basis.
(b) Before conversion of off-balance-sheet components to credit (e.g., taking into account unutilized credit lines), before credit risk mitigation through certain actions (for example, through guarantees) and after netting derivative transactions.
(c) Including loans to the public, loans to the government and deposits with central banks, and after deducting liabilities for transactions in derivatives subject to CSA agreements.
(d) Excluding the debentures in the marketable portfolio and excluding capital investments in financial institutions.
(e) Including cash, investments in financial institutions which have not been deducted from capital, tax prepayments, shares and other assets without a counterparty, such as: buildings and equipment.
(f) Positive fair value of derivatives, including an add-on that reflects the potential amount of the future exposure to credit in respect of the balance of the derivative instruments' par value and after netting derivative transactions.

Table 21 - Breakdown of the portfolio by repayment period and main type of exposure (Pillar 3)[(a)]

	December 31 2017					
	Credit[(c)]	Debentures[(d)]	Other[(e)]	Guarantees and other commitments	Transactions in derivatives[(f)]	Total[(b)]
	in NIS millions					
Up to 12 months	**167,109**	**39,389**	**4,757**	**72,357**	**5,010**	**288,622**
More than 12 months and up to 5 years	**83,327**	**13,794**	**1,531**	**32,421**	**5,254**	**136,327**
Over five years	**97,539**	**16,602**	**3,825**	**21,341**	**3,392**	**142,699**
Non-monetary items	**396**	**-**	**7,933**	**-**	**11,785**	**20,114**
Benefits for offsetting	**-**	**-**	**-**	**-**	**(11,549)**	**(11,549)**
Total	**348,371**	**69,785**	**18,046**	**126,119**	**13,892**	**576,213**

	December 31 2016					
	Credit[(c)]	Debentures[(d)]	Other[(e)]	Guarantees and other commitments	Transactions in derivatives[(f)]	Total[(b)]
	in NIS millions					
Up to 12 months	156,811	35,592	4,266	72,142	4,576	273,387
More than 12 months and up to 5 years	80,714	17,302	1,409	32,146	5,701	137,272
Over five years	98,666	14,717	4,141	20,254	4,306	142,084
Non-monetary items	464	-	6,837	-	5,619	12,920
Benefits for offsetting	-	-	-	-	(11,737)	(11,737)
Total	336,655	67,611	16,653	124,542	8,465	553,926

(a) After deducting write-offs and before deducting credit loss allowances on an individual and collective basis.
(b) Before conversion of off-balance-sheet components to credit (e.g., taking into account unutilized credit lines), before credit risk mitigation through certain actions (for example, through guarantees) and after netting derivative transactions.
(c) Including loans to the public, loans to the government and deposits with central banks, and after deducting liabilities for transactions in derivatives subject to CSA agreements.
(d) Excluding the debentures in the marketable portfolio and excluding capital investments in financial institutions.
(e) Including cash, investments in financial institutions which have not been deducted from capital, tax prepayments, shares and other assets without a counterparty, such as: buildings and equipment.
(f) Positive fair value of derivatives, including an add-on that reflects the potential amount of the future exposure to credit in respect of the balance of the derivative instruments' par value and after netting derivative transactions.

Credit risk mitigation

Policy and processes regarding valuation and collaterals management

Under its credit risk management policy, the Bank's main consideration when providing credit is a borrower's repayment capacity. Therefore, in many cases, the Bank strives to obtain collateral as additional backup, so as to reduce loss to the Bank in the event of a borrower's business- or financial failure. The value of collateral is derived, inter alia, from a borrower's credit risk level.

As part of its collateral policy for all industries, the Bank has set principles and rules regarding collateral types and amounts. Collateral requirements and rates derive from the level of risk the Bank is willing to assume when granting a loan.

Furthermore, business criteria are determined on receiving a collateral as well as the rate of reliance on the collateral, its handling, methods and timing for updating its value and means of control and monitoring.

As far as possible, collateral is adapted to the kind of credit it secures, taking into account the time frame, types of linkage, nature and purpose of the credit, as well as the speed in which the collateral can be realized. The Bank verifies the value of the main collateral (particularly in the real estate and equipment fields) by obtaining independent, up-to-date appraisals or valuations.

The most common types of collateral the Bank accepts to secure credit include, inter alia, financial assets, real estate properties, motor vehicles, various types of equipment, etc.

The Bank has a computerized system which can generate information regarding the type of assets used as collateral.

For more information on credit risk mitigation, please see below under "Disclosure under the standardized approach".

Portfolios managed according to the standardized approach

The risk for credit exposures is weighted based on the standardized approach. Under this approach, risk weightings depend on exposure types, and in some cases, rely on associated credit ratings (insofar as an eligible rating is available). In case such exposures have ratings as foregoing, the Bank uses the credit ratings of three external credit rating agencies:

- Standard & Poor's Ratings Services
- Moody's Investors Service
- Fitch Ratings

The risk weightings of debts based on country ratings which include exposures to governments, banks, securities issuers and public-sector entities are determined on the basis of Moody's long-term credit ratings.
Risk weightings for debts of rated corporations are determined on the basis of the long-term credit ratings of these corporations, in the following manner: When the debt has a single rating, that rating is used to determine the debt's risk weighting. When there are two ratings, by two different agencies, mapped for different risk weightings, the higher risk weighting is selected. When three ratings are available, the best two ratings will be taken into account, and from these, the risk weighting referring to the lower rating of the two will be selected.

On October 22, 2017, a circular was published revising Proper Conduct of Banking Business Directive No. 203. The main purpose of the revision was to expand the list of eligible external credit assessment institutions (ECAI) for the purpose of determining the risk weightings and calculating capital requirements for credit exposures. The revision added AM Best Europe-Rating Services and the IFS/financial strength rating was added to the eligible ratings map, which is used to rate the exposures of insurance companies in Europe and the USA. The revision was made following banking corporations' purchase of insurance policies for collateral portfolios pursuant to the Sales Law, as well as for other portfolios.

On all matters relating to the risk weightings for the debts of corporations that are insurers or reinsurers, the Bank uses the long-term IFS (financial strength) ratings of the rating agencies.

In addition, the list of primary indices for the purpose of determining collaterals' eligibility was updated. Thus, as part of the revised directive, the Euro Stoxx 50 was added to the primary index list, and the Tel Aviv 100 index was updated to the Tel Aviv 125 index.

The foregoing updates had no material effect on the Bank's capital adequacy ratio.

In order to determine the risk weightings in accordance with the credit ratings as foregoing, the Bank uses the standardized mapping tables prescribed by the Banking Supervision Department under Proper Conduct of Banking Business Directive No. 203. The following tables outline credit exposures by their risk weightings, while segmenting the exposure according to the counterparty, after allowances for credit losses and before and after mitigating the credit risk for known collaterals.

Table 22 - Amount of exposure after expenses in respect of credit losses and before credit risk mitigation (Pillar 3)

	December 31 2017					
	0%	20%	35%	40%	50%	75%
	in NIS millions					
Sovereign debts	**113,353**	**4,558**	**-**	**-**	**731**	**-**
Debts of public sector	**-**	**9,454**	**-**	**-**	**6,313**	**-**
Debts of banking	**3,622**	**19,274**	**-**	**-**	**3,189**	**-**
Debts of securities issuers	**-**	**1,869**	**-**	**-**	**-**	**-**
Debts of corporations	**-**	**2,945**	**-**	**-**	**842**	**-**
Debt collateralized by	**-**	**-**	**-**	**-**	**-**	**-**
Retail exposures to	**-**	**-**	**-**	**-**	**-**	**74,787**
Loans to small businesses	**-**	**-**	**-**	**-**	**-**	**23,187**
Housing mortgages	**-**	**-**	**29,876**	**-**	**16,837**	**32,027**
Securitization	**-**	**2,514**	**-**	**19**	**159**	**-**
Other assets	**3,539**	**-**	**-**	**-**	**-**	**-**
Total	**120,514**	**40,614**	**29,876**	**19**	**28,071**	**130,001**

(a) Before conversion of off-balance-sheet components to credit (e.g., taking into account unutilized credit lines), before credit risk mitigation through certain actions (for example, through guarantees) and after netting derivative transactions.

* As of January 1 2017, changes have been made in the calculation of exposures to major counterparties. In accordance with revised Proper Conduct of Banking Business Directive No. 203, the exposure to the stock exchange was risk-weighted at 20%.

For more information, please see the note on capital adequacy in the financial statements.

100%	150%	225%	250%	350%	650%	1250%	Gross credit exposure[(a)]
990	**-**	**-**	**-**	**-**	**-**	**-**	**119,632**
10	**-**	**-**	**-**	**-**	**-**	**-**	**15,777**
656	**31**	**-**	**-**	**-**	**-**	**-**	**26,772**
-	**-**	**-**	**-**	**-**	**-**	**-**	**1,869**
131,145	**1,611**	**-**	**-**	**-**	**-**	**-**	**136,543**
73,840	**291**	**-**	**-**	**-**	**-**	**-**	**74,131**
81	**245**	**-**	**-**	**-**	**-**	**-**	**75,113**
36	**205**	**-**	**-**	**-**	**-**	**-**	**23,428**
2,619	**214**	**-**	**-**	**-**	**-**	**-**	**81,573**
-	**-**	**-**	**-**	**-**	**-**	**-**	**2,692**
9,102	**583**	**-**	**4,822**	**-**	**-**	**-**	**18,046**
218,479	**3,180**	**-**	**4,822**	**-**	**-**	**-**	**575,576**

	December 31 2016					
	0%	20%	35%	40%	50%	75%
	in NIS millions					
Sovereign debts	111,849	3,454	-	-	261	-
Debts of public sector	-	8,810	-	-	5,736	-
Debts of banking	2,847	13,550	-	-	2,334	-
Debts of securities issuers	-	1,121	-	-	-	-
Debts of corporations	-	1,781	-	-	1,276	-
Debt collateralized by	-	-	-	-	-	-
Retail exposures to	-	-	-	-	-	74,471
Loans to small businesses	-	-	-	-	-	21,214
Housing mortgages	-	-	33,100	-	15,181	31,440
Securitization	-	2,931	-	78	26	-
Other assets	2,876	-	-	-	-	-
Total	117,572	31,647	33,100	78	24,814	127,125

(a) Before conversion of off-balance-sheet components to credit (e.g., taking into account unutilized credit lines), before credit risk mitigation through certain actions (for example, through guarantees) and after netting derivative transactions.

100%	150%	225%	250%	350%	650%	1250%	Gross credit exposure[a]
786	-	-	-	-	-	-	116,350
44	-	-	-	-	-	-	14,590
498	18	-	-	-	-	-	19,247
-	-	-	-	-	-	-	1,121
130,537	1,578	-	-	-	-	-	135,172
68,275	268	-	-	-	-	-	68,543
36	25	-	-	-	-	-	74,532
9	54	-	-	-	-	-	21,277
2,630	213	-	-	-	-	-	82,564
-	-	-	-	-	-	-	3,035
8,996	479	-	4,302	-	-	-	16,653
211,811	2,635	-	4,302	-	-	-	553,084

Table 23 - Exposure amount after expenses in respect of credit losses and before credit risk mitigation (Pillar 3)[b]

	December 31 2017					
	0%	20%	35%	40%	50%	75%
	in NIS millions					
Sovereign debts	**121,510**	**4,581**	**-**	**-**	**731**	**-**
Debts of public sector	**1,527**	**3,537**	**-**	**-**	**6,310**	**-**
Debts of banking	**3,622**	**17,792**	**-**	**-**	**1,719**	**-**
Debts of securities issuers	**-**	**1,462**	**-**	**-**	**-**	**-**
Debts of corporations	**-**	**21,402**	**-**	**-**	**4,508**	**-**
Debt collateralized by	**-**	**-**	**-**	**-**	**-**	**-**
Retail exposures to	**-**	**-**	**-**	**-**	**-**	**73,823**
Loans to small businesses	**-**	**-**	**-**	**-**	**-**	**21,291**
Housing mortgages	**-**	**-**	**29,877**	**-**	**16,837**	**31,987**
Securitization	**-**	**1,772**	**-**	**19**	**159**	**-**
Other assets	**3,539**	**-**	**-**	**-**	**-**	**-**
Total	**130,198**	**50,546**	**29,877**	**19**	**30,264**	**127,101**

(a) Before conversion of off-balance-sheet components to credit (e.g., taking into account unutilized credit lines), after credit risk mitigation through certain actions (for example, through guarantees) and after netting derivative transactions.

(b) Credit risk mitigation expresses a classification of the final risk weighting between the various rates.

* As of January 1 2017, changes have been made in the calculation of exposures to major counterparties. In accordance with revised Proper Conduct of Banking Business Directive No. 203, the exposure to the stock exchange was risk-weighted at 20%.

For more information, please see the note on capital adequacy in the financial statements.

100%	150%	225%	250%	350%	650%	1250%	Gross credit exposure[(a)]
771	**-**	**-**	**-**	**-**	**-**	**-**	**127,593**
10	**-**	**-**	**-**	**-**	**-**	**-**	**11,384**
636	**3**	**-**	**-**	**-**	**-**	**-**	**23,772**
-	**-**	**-**	**-**	**-**	**-**	**-**	**1,462**
99,344	**1,603**	**-**	**-**	**-**	**-**	**-**	**126,857**
73,264	**291**	**-**	**-**	**-**	**-**	**-**	**73,555**
70	**245**	**-**	**-**	**-**	**-**	**-**	**74,138**
34	**205**	**-**	**-**	**-**	**-**	**-**	**21,530**
2,618	**214**	**-**	**-**	**-**	**-**	**-**	**81,533**
-	**-**	**-**	**-**	**-**	**-**	**-**	**1,950**
9,102	**583**	**-**	**4,822**	**-**	**-**	**-**	**18,046**
185,849	**3,144**	**-**	**4,822**	**-**	**-**	**-**	**561,820**

	December 31 2016					
	0%	20%	35%	40%	50%	75%
	in NIS millions					
Sovereign debts	119,244	3,423	-	-	261	-
Debts of public sector	1,333	3,676	-	-	5,644	-
Debts of banking	2,847	10,704	-	-	2,278	-
Debts of securities issuers	-	863	-	-	-	-
Debts of corporations	-	20,135	-	-	5,207	-
Debt collateralized by	-	-	-	-	-	-
Retail exposures to	-	-	-	-	-	73,170
Loans to small businesses	-	-	-	-	-	19,384
Housing mortgages	-	-	33,099	-	15,181	31,400
Securitization	-	2,203	-	78	26	-
Other assets	2,876	-	-	-	-	-
Total	126,300	41,004	33,099	78	28,597	123,954

(a) Before conversion of off-balance-sheet components to credit (e.g., taking into account unutilized credit lines), after credit risk mitigation through certain actions (for example, through guarantees) and after netting derivative transactions.

100%	150%	225%	250%	350%	650%	1250%	Gross Credit exposure[(a)]
274	-	-	-	-	-	-	123,202
44	-	-	-	-	-	-	10,697
498	2	-	-	-	-	-	16,329
-	-	-	-	-	-	-	863
98,838	1,571	-	-	-	-	-	125,751
67,744	268	-	-	-	-	-	68,012
28	25	-	-	-	-	-	73,223
9	53	-	-	-	-	-	19,446
2,630	213	-	-	-	-	-	82,523
-	-	-	-	-	-	-	2,307
8,996	479	-	4,302	-	-	-	16,653
179,061	2,611	-	4,302	-	-	-	539,006

Credit risk mitigation - Disclosures under the standardized approach

In order to mitigate the credit risk under the standardized approach, the Bank employs the comprehensive method for handling collaterals.

The main instruments recognized as valid collateral by the Bank under the standardized approach are shekel deposits, foreign currency deposits, savings plans and government bonds.

A collateral is recognized as valid when it meets the requirements of Proper Conduct of Banking Business Directive No. 203, including legal certainty, the right to early call back in case of credit failure and applicability to third parties.

The Bank uses netting letters that meet the terms and conditions set forth in Proper Conduct of Banking Business Directive No. 203, in order to use the net exposure of loans and deposits as the basis for calculating capital adequacy.

In addition, the Bank employs a netting set in derivative transactions, pursuant to Appendix C to the foregoing Directive No. 203 in derivative transactions for which there are bipartite account settling agreements in effect. To mitigate the credit risk in derivative transactions, the Bank enters CSAs (credit support annex - agreements for offsetting and settling accounts for derivatives) and collateral transfer agreements with banks and customers.

To change the risk weighting of debts backed by guarantees to the risk weighting of the security provider, when calculating the risk assets under the standardized approach, the Bank recognizes mainly the following types of collateral as valid - government guarantees, guarantees by Israeli banks and credit guarantees and insurance policies by reinsurers, which are similar in nature and which meet the validity criteria for capital adequacy purposes.

Table 24 - Credit risk mitigation (Pillar 3)

	December 31 2017					
	Gross credit exposure before allowances for credit losses[(a)]	Gross credit exposure after allowances for credit losses[(a)]	Total exposure covered by de-recognized guarantees	Total amounts added	Total exposure covered by valid financial collateral[(b)]	Net credit exposure[(c)]
	in NIS millions					
Sovereign debts	**119,632**	**119,632**	**(432)**	**8,393**	**-**	**127,593**
Debts of public sector entities	**15,777**	**15,777**	**(5,917)**	**1,527**	**(3)**	**11,384**
Debts of banking corporations	**26,772**	**26,772**	**(1,907)**	**445**	**(1,538)**	**23,772**
Debts of securities issuers	**1,869**	**1,869**	**-**	**-**	**(407)**	**1,462**
Debts of corporations	**136,925**	**136,543**	**(23,701)**	**22,475**	**(8,460)**	**126,857**
Debt collateralized by commercial properties	**74,137**	**74,131**	**(109)**	**-**	**(467)**	**73,555**
Retail exposures to individuals	**75,131**	**75,113**	**(1)**	**-**	**(974)**	**74,138**
Loans to small businesses	**23,484**	**23,428**	**(23)**	**-**	**(1,875)**	**21,530**
Housing mortgages	**81,748**	**81,573**	**(8)**	**-**	**(32)**	**81,533**
Securitization	**2,692**	**2,692**	**(742)**	**-**	**-**	**1,950**
Other assets	**18,046**	**18,046**	**-**	**-**	**-**	**18,046**
Total for credit risk	**576,213**	**575,576**	**(32,840)**	**32,840**	**(13,756)**	**561,820**

(a) Before conversion of off-balance-sheet components to credit (e.g., taking into account unutilized credit lines), before credit risk mitigation through certain actions (for example, through guarantees) and after netting derivative transactions.
(b) After taking into account buffers.
(c) Before conversion of off-balance-sheet components to credit (e.g., taking into account unutilized credit lines), after credit risk mitigation and after netting derivative transactions.

	December 31 2016					
	Gross credit exposure before allowances for credit losses[(a)]	Gross credit exposure after allowances for credit losses[(a)]	Total exposure covered by derecognized guarantees	Total amounts added	Total exposure covered by valid financial collateral[(b)]	Net credit exposure[(c)]
	in NIS millions					
Sovereign debts	116,350	116,350	(560)	7,412	-	123,202
Debts of public sector	14,590	14,590	(5,203)	1,333	(23)	10,697
Debts of banking	19,247	19,247	(1,957)	414	(1,375)	16,329
Debts of securities issuers	1,121	1,121	-	-	(258)	863
Debts of corporations	135,738	135,172	(23,084)	22,457	(8,794)	125,751
Debt collateralized by	68,552	68,543	(42)	-	(489)	68,012
Retail exposures to	74,557	74,532	(4)	-	(1,305)	73,223
Loans to small businesses	21,331	21,277	(22)	-	(1,809)	19,446
Housing mortgages	82,752	82,564	(16)	-	(25)	82,523
Securitization	3,035	3,035	(728)	-	-	2,307
Other assets	16,653	16,653	-	-	-	16,653
Total for credit risk	553,926	553,084	(31,616)	31,616	(14,078)	539,006

(a) Before conversion of off-balance-sheet components to credit (e.g., taking into account unutilized credit lines), before credit risk mitigation through certain actions (for example, through guarantees) and after netting derivative transactions.
(b) After taking into account buffers.
(c) Before conversion of off-balance-sheet components to credit (e.g., taking into account unutilized credit lines), after credit risk mitigation and after netting derivative transactions.

Exposures related to derivative counterparty risk

The credit risk embodied in a derivative transaction is a measure of the loss the Bank may incur if the counterparty to the transaction fails to meet the terms of the transaction. Such risk, per a specific date, is defined as the total present value of the transaction as at that date plus the potential risk for a future loss. The potential is evaluated by the level of the underlying asset's expected volatility and the period remaining until the completion of the collateral as agreed with the customer. The credit risk may also be measured according to the maximum loss amount, under scenarios, the Bank may incur, less enforceable offsetting clauses.

The developments in global currency markets and foreign exchange rate volatility in various currencies, as well as their implications for active foreign currency borrowers, require monitoring, supervision and control of customers' exposures to market price fluctuations (foreign exchange rates, inflation rates, etc.). To this end, there are guidelines addressing the necessary adjustment between a loan's underlying currency and the cash flow currency constituting the source of repayment for that loan; there is also awareness of the currency risk exposure as well as added focus on borrowers with high exposure potential. Where necessary, the borrower's risk rating is updated and a demand is made for the borrower to boost its equity and collateral base.

If a borrower is found to have exposure or sensitivity to changes in foreign exchange rates and/or commodity prices, the party in charge at the Bank is required to evaluate the borrower's overall sensitivity, taking into account all the criteria for including the borrower in the sensitive customers list, as well as weighting and quantifying the borrowers' sensitivity to changes in the foreign exchange rates and/or commodity prices as embodied in their activity.

The Bank's Capital Markets Division is in charge of customers' activities in all types of derivatives. This Division closely monitors customers who are active in the financial and capital markets, as well as such activity carried out by other customers of the Bank. The Division is responsible for the models for calculating the collateral requirement, the criteria used by these models, the IT systems which measure compliance with the boundaries of the activity and the work procedures.

In recent years, mechanisms for credit risk mitigation of transactions between counterparties have been developed, by recognizing the effect of netting processes anchored in standard global legal agreements (such as ISDAs) as well as a mechanism for posting mutual collateral between counterparties to a transaction (CSA agreements). All of the Bank's inter-bank trading activity is performed only vis-à-vis counterparties with whom it has such agreements. In addition, such agreements are increasingly entered into with customers that have extensive derivative activities.

For CSA agreements with other banks, market data and exposure are calculated and accounted for on a daily basis. The security is in cash and the amount is stated in the currency specified in the agreement.

Table 25 - Balances of credit risk for counterparties in derivatives (Pillar 3)

	December 31			
	2017		2016	
	Balance of nominal value	Net credit exposures to derivatives	Balance of nominal value	Net credit exposures to derivatives
	in NIS millions			
Interest rate contracts	**286,840**	**6,296**	331,589	7,859
foreign exchange rate contracts	**243,635**	**6,567**	252,529	6,727
Stock contracts	**181,057**	**12,499**	104,127	5,537
Commodity and other contracts	**539**	**80**	610	79
Credit derivative transactions[(a)]	**-**	**-**	-	-
Offsetting benefits	**-**	**(11,550)**	-	(11,737)
Eligible collateral	**-**	**(4,752)**	-	(3,682)
Total	**712,071**	**9,140**	688,855	4,783

(a) As of the report date, there are no credit risk exposures to sold or purchased hedging.

Securitization

The Bank does not securitize its assets.
However, the Bank does invest in asset-backed securities through its own account, as follows:
Asset-backed securities are characterized by wide diversification of borrowers and sometimes also by industry and inter-industry diversification. In addition, for some instruments, there are several risk layers, which allow the Bank to be flexible when adapting an investment to its risk appetite.
Investments in various types of asset-backed securities are evaluated in advance both in terms of expected returns and inherent risk.

The Bank's own investment portfolio

Table 26 - Available-for-sale portfolio - investment in mortgage-backed and asset-backed securities by type of exposure (Pillar 3)

	December 31					
	2017			2016		
	Amortized cost	Accumulated other compre-hensive income (loss)	Fair value	Amortized cost	Accumulated other comprehensive income (loss)	Fair value
	in NIS millions					
Mortgage-backed securities (MBSs)						
Pass-through type available-for-sale securities	**3,036**	**(35)**	**3,001**	3,063	(76)	2,987
Of which: GNMA-backed securities	**326**	**(8)**	**318**	281	(8)	273
Securities issued by FNMA and by FHLMC	**1,960**	**(19)**	**1,941**	2,039	(53)	1,986
Other mortgage-backed securities (Including CMOs and Stripped MBSs)	**3,960**	**(35)**	**3,925**	5,083	(85)	4,998
Of which: securities issued or guaranteed by GNMA ,FNMA ,FHLMC	**3,800**	**(36)**	**3,764**	4,539	(84)	4,455
Total MBSs	**6,996**	**(70)**	**6,926**	8,146	(161)	7,986
Asset-backed securities (ABSs)						
Other consumer credit	**-**	**-**	**-**	332	4	338
Other non-consumer credit	**-**	**-**	**-**	1	-	1
CLO-type debentures	**1,599**	**4**	**1,603**	1,413	14	1,424
Total asset-backed securities (ABSs)	**1,599**	**4**	**1,603**	1,746	18	1,763
Total available-for-sale mortgage-backed and asset-backed securities	**8,595**	**(66)**	**8,529**	9,892	(143)	9,749

Table 27 - Available-for-sale portfolio - investment in mortgage-backed and asset-backed securities by risk weighting (Pillar 3)[(a)]

	December 31 2017			
	Aggregate exposure amount			
	Securitization exposures	Resecuritization exposures	Total	Capital requirements for securitization exposures
	in NIS millions			
20%	**2,328**	**-**	**2,328**	**64**
40%	**-**	**19**	**19**	**1**
50%	**159**	**-**	**159**	**30**
100%	**-**	**-**	**-**	**-**
225%	**-**	**-**	**-**	**-**
1250%	**-**	**-**	**-**	**-**
Total	**2,487**	**19**	**2,506**	**95**

	December 31 2016			
	Aggregate exposure amount			
	Securitization exposures	Resecuritization exposures	Total	Capital requirements for securitization exposures
	in NIS millions			
20%	2,931	-	2,931	73
40%	-	78	78	4
50%	26	-	26	2
100%	-	-	-	-
225%	-	-	-	-
1250%	-	-	-	-
Total	2,957	78	3,035	79

*(a) Excluding FNMA and FHLMC securities risk-weighted at 20%. Excluding GNMA securities risk-weighted at 0%.

Table 28 - Held-to-maturity portfolio - investment in mortgage-backed and asset-backed securities by type of exposure (Pillar 3)[(a)]

	December 31	
	2017	2016
	Total balance of exposure	
	in NIS millions	
Mortgage-backed securities (MBSs)		
Other mortgage-backed securities (including CMOs and Stripped MBSs)	**347**	-
Of which: Securities issued or guaranteed by FHLMC,FNMA or GNMA	**163**	-
Total MBSs	**347**	-
Total asset-backed securities for held-to-maturity	**347**	-

(a) The Bank was given permission to reclassify the debentures in the held-to-maturity portfolio from January 1, 2017. Consequently, the Bank reclassified debentures of a foreign subsidiary from the available-for-sale portfolio to the held-to-maturity portfolio in the amount of NIS 957 million, of which NIS 466 million are asset-backed securities.
Under the Bank of Israel's directives, when reclassifying debentures from the available-for-sale portfolio to the held-to-maturity portfolio, unrealized gains or losses as at the reclassification date continue to be presented in shareholders' equity, but from that date onwards - are amortized over the remaining life of the debentures. The loss amount in the capital reserve as at the reclassification date is approximately NIS 35 million.

Table 29 - Held-to-maturity portfolio - investment in mortgage-backed and asset-backed securities by risk weighting (Pillar 3)[(a)]

	December 31 2017			
	Aggregate exposure amount			
	Securitization exposures	Resecuritization exposures	Total	Capital requirements for securitization exposures
	in NIS millions			
20%	**186**	**-**	**186**	**5**
40%	**-**	**-**	**-**	**-**
50%	**-**	**-**	**-**	**-**
100%	**-**	**-**	**-**	**-**
225%	**-**	**-**	**-**	**-**
1250%	**-**	**-**	**-**	**-**
Total	**186**	**-**	**186**	**5**

(a) Excluding FNMA and FHLMC securities risk-weighted at 20%. Excluding GNMA securities risk-weighted at 0%.

Trading portfolio

Table 30 - Trading portfolio - investment in mortgage-backed and asset-backed securities by type of exposure (Pillar 3)

	December 31					
	2017			2016		
	Amortized cost	Accumulated other comprehensive income (loss)	Fair value	Amortized cost	Accumulated other comprehensive income (loss)	Fair value
	in NIS millions					
Pass-through type held-for-trading securities	**4**	**-**	**4**	6	-	6
Of which: Securities issued by FNMA or FHLMC	**4**	**-**	**4**	6	-	6
Other mortgage-backed securities (Including CMOs and Stripped MBSs)	**54**	**-**	**54**	86	-	86
Of which: Securities issued or guaranteed by FNMA, FHLMC or GNMA	**-**	**-**	**-**	-	-	-
Total MBSs	**58**	**-**	**58**	92	-	92
Total asset-backed securities (ABSs)	**209**	**1**	**210**	188	-	188
Total mortgage-backed and asset-backed securities for trading	**267**	**1**	**268**	280	-	280

Table 31 - Trading portfolio - investment in mortgage-backed and asset-backed securities by risk weighting (Pillar 3)[(a),(b)]

	December 31			
	2017		2016	
	Aggregate exposure amount	Capital requirements for securitization exposures	Aggregate exposure amount	Capital requirements for securitization exposures
	in NIS millions			
20%	**144**	**4**	149	4
50%	**118**	**8**	121	8
100%	**-**	**-**	1	-
350%	**2**	**1**	3	1
1250%	**0**	**1**	0	-
Total	**264**	**14**	274	13

(a) Excluding FNMA and FHLMC securities risk-weighted at 20%. Excluding GNMA securities risk-weighted at 0%.
(b) As at December 31 2016, there were no resecuritization positions in the financial statements.

Market risk

Market risk is defined as the risk of loss in balance sheet and off-balance sheet positions as a result of a change in the fair-value of a financial instrument due to change in market conditions (i.e., changes in: price levels in various markets; interest rate volatility; foreign exchange rates; inflation rates; share prices and commodities, as well as in other economic measures). Market risk exposure is reflected in the financial performance, in the fair value of the assets and liabilities, in shareholders' equity and in cash flows.

The market risks to which the Bank is exposed include the following (for more information, please see below):

a. Interest rate risk is the risk of loss as a result of changes in risk-free interest rates across various currencies.
b. Basis risk (foreign exchange rates and CPI) is the risk of loss as a result of changes in the consumer price index or foreign exchange rates, due to the difference between the value of the assets and the value of the liabilities, including in respect of future transactions in each of the linkage bases.
c. Tradable credit risk, caused by credit spread volatility derived from the instrument issuer's repayment capacity or from changes in the overall risk of tradable debt instruments.
d. Risk of investment in shares and funds, caused by impairment of the investment in shares or funds or a decrease in profits or dividends paid to the Group.

The Bank complies with the Supervision of Banks Department's directives regarding the management of the Group's market risks, including Proper Conduct of Banking Business Directive No. 333, *Interest Rate Risk Management*, and No. 339, *Market Risk Management*. To implement these directives, the Bank established basic principles and control mechanisms for these risks, including the purviews of management and the Board of Directors, defining the means of control and tools for measuring risk and the means of control and oversight of these risks, while implementing corporate governance with three lines of defense.

Organizational structure and responsibility for market risk management

First line of defense - Capital Markets Division

The Capital Markets Division is responsible for assuming the risk while analyzing and understanding it throughout the transaction's life. The Division manages the Bank's own account and operates all of its trading rooms - which are responsible for trading and arbitrating in currencies, interest rates, derivatives and securities. In addition, the Division handles the Group's financial management, including developing financial and investment products and managing the Group's assets and liabilities. The Division is also responsible for: keeping contact with foreign financial institutions; providing service to customers who are active in the capital and money markets, including institutionals; and ongoing risk control management of the foregoing activities. In addition to the control processes built into the trading rooms, ongoing monitoring of market risks, operational risks and embezzlement and fraud risks is conducted by the Planning Room of the Division's risk management department. The Capital Markets Division - which serves as the first line of defense - is aided by Leumi's investment arm – Leumi Partners.

Second line of defense - Risk Management Division

The Division is responsible for examining the market and liquidity risks management from a comprehensive perspective, through: involvement in assessing the risks embodied in new products and activities as well as formulating the risk policy and risk boundaries from an overall perspective of the Bank's own account and trading rooms, the Bank's nonbanking investments and its pension portfolio. It is also responsible for developing and challenging risk assessments of material transactions and activities, such as approval of products, investments, and new transactions; developing methodologies; validating material models; monitoring market variables and specific investments; and conducting stress scenarios, etc.

Third line of defense - Internal Audit

The Internal Audit Division is responsible to retroactively examine whether the risk management processes of the first and second lines of defense are intact and efficient and expose any internal control vulnerabilities.

Market risk management is discussed by the following committees:

a. Board of Directors' Risk Management Committee - each quarter, the Board of Directors' Risk Management Committee discusses the Risk Management Division's risk paper, which includes credit risk exposures, and an overview of compliance with the boundaries at the Group and Bank levels. The Committee receives a report on the updated status of compliance with the restrictions at the Group level, as well as possible damage to the Bank under stress scenarios. Any highly material new activity in financial instruments is presented to the Committee for discussion and approval, as part of the "new product" procedure. In addition, once a year, the market risk management policy paper is presented for the Committee's discussion and approval, and the recommendations of the Board of Directors' Risks Management Committee are submitted to the Board of Directors plenary for approval.

b. The Executive Risk Committee, headed by the CEO, discusses the policy and material topics related to market risks after they have been discussed by the Executive Credit Risk Committee.

c. The Asset-Liability Committee (ALCO), led by the Head of the Capital Markets Division, is responsible for managing the assets, liabilities and financial investments according to the decisions of the Board of Directors and management, with focus on balance sheet structure, transfer prices, required liquidity and liquidity reserve investments, capital structure and the policy for raising financing resources and meeting the Group's restrictions and policies.

d. The Executive Market Risk Committee, headed by the Chief Risk Manager, examines market events and trends which may affect the Bank and is responsible for discussing and approving the risk policy and restrictions – prior to presenting them to the Board of Directors for discussion and approval; to monitor compliance with the said restrictions and to approve the methodology for measuring the Leumi Group's exposure to market risk.

Market risk management policy

The Market risk management policy is an expression of the Group's market risk strategy, alongside existing procedures for identifying, measuring, monitoring, developing and controlling market risk. The policy is designed, on the one hand, to support the achievement of business targets while assessing the risks and rewards that may arise from exposure to the risks compared with the expected gains therefrom and, on the other hand, to mitigate the risk level arising from the Bank's ongoing activities, including by maintaining a high level of liquidity.

The policy constitutes an important tool for defining the Bank's risk appetite for its own account, trading rooms and market exposure across the entire Leumi Group. The policy outlines the corporate governance, division of organizational responsibility and escalation mechanisms.

The market risks are routinely managed at a Group level. The foreign subsidiaries determine their market risk management policies in line with the Group's policies and its approved risk frameworks. Information on the actual exposure status according to the established frameworks is reported by the subsidiaries and taken into account in the overall management of the Group's exposures.

Market risk management is performed in two risk centers – the banking portfolio and the trading portfolio. The definition of the trading portfolio is derived from the Basel rules and includes the Bank's tradable securities portfolio and derivative transactions as part of its trading activity. The banking portfolio includes those trading transactions which are not included in the trading portfolio.

Exposure to market risks arising from employee pension obligations

The Bank applies the US GAAP for employee benefits, as prescribed by the Bank of Israel. Managing the market risks in respect of the obligations for employees is partly performed as part of the banking portfolio and partly in an independent and separate manner vis-a-vis the management of plan assets, which was designed to yield long term returns to serve the obligation's value. The long-duration actuarial obligation to employees is significantly impacted by changes in the discount interest. The discount rate, which is used for calculating the actuarial liabilities for employee rights, is based on the Government of Israel's debenture yield curve plus the fixed spread curve of internally AA-graded corporate debentures which match the durations of the liabilities for employee rights.

The banking portfolio

The market risks embodied in the banking portfolio arise from the Bank's core activities (primarily credit, deposits and securities investments in the available-for-sale portfolio). The portfolio's main market risks are interest rate risk and the basis asset risk exposures. The main tools for managing the exposures in the banking portfolio are: the price policy; the management of the Bank's own available-for-sale portfolio; the issue of debt instruments; and hedging by way of derivatives. The hedging policy enables to narrow down and/or expand risk, as needed, by changing the Bank's position in accordance with the risk appetite defined by the Board of Directors.

The investment policy

Leumi's own account activity constitutes a principal tool for managing the assets and liabilities, balance linkages, routing exposed capital and generating profits. It is managed using an overall perspective, including reference to all risks and opportunities, including the own account portfolios, the non-banking holdings and assets and the liabilities in the pension portfolio. The investment policy is also subject to risk appetite restrictions set by the Board of Directors. The principal risks embodied in the investment activity are interest rate, credit, liquidity and basis risks.

To maintain stability and a high level of liquidity, assets are managed by assuming a low to moderate risk for most investments and activities and assuming a higher risk for a smaller part of the investments and activities. Under the policy, a high level of diversification is maintained across products, countries, and types of risk and exposures to counterparties.

In its own portfolios, Leumi is exposed to credit and market risks in respect of countries, banks and financial institutions in Israel and abroad. The Bank also limits investments in asset-backed instruments (such as MBSs, CLOs, ABSs and others) as well as to highly diversified funds and shares.

For investments in entities whose main business is derivative financial instruments and short sales (hedge funds), quantitative limitations regarding the investment amount were set, in accordance with the risk profile. In addition, extensive due diligence testing is conducted, as are control circles and corporate governance processes, based on reporting and measuring mechanisms.

As part of examining its overall risk profile, the Bank regularly performs follow ups and monitors the exposures to market risks and losses that may occur under different scenarios, including stress scenarios, in order to reflect the overall market risks from a holistic perspective – risks of interest, basis, credit margins, shares and funds.

Leumi has defined alert mechanisms for exceptional developments in the exposure status and/or markets, including:

- Setting reporting thresholds regarding deviations from quantitative restrictions, reporting methods and providing alternatives to handle deviations.
- Follow up mechanisms (watch lists) and red flags, which monitor market developments, compliance with restrictions, changes in assets, etc.

Leumi has drafted detailed contingency plans that include action plans in case predefined triggers are activated.

The trading portfolio

The market risks embodied in the trading portfolio arise from the Bank's activity as a market maker, broker and positions manager for its own account, for the purpose of generating profits from trading, while quickly responding to market changes.

Leumi trades in a very broad range of derivatives with various underlying assets: currencies, interest rates, index, commodities and securities. Most of the activity is performed in common and highly liquid instruments in the local and global markets.
In the framework of Bank’s own trading portfolio, proactive actions are taken such as proactive exposures to interest, foreign currencies and tradable credit risks.
Almost daily, market risks in the trading portfolio are identified, monitored, and controlled against the restrictions - by the Capital Markets Division’s control unit.

Risk-measuring methodologies and tools

Market risks are estimated using a variety of tools, which complement each other and are in line with the Bank’s various exposures. The measures used by the Bank for its overall management of market risks are also used for evaluating the potential financial damage from overall market and tradable credit exposures or from a specific portfolio having such exposures, under assumptions which take into account the interrelations between the various risk factors embodied in each portfolio and collectively - in all of them.

The Bank’s market risk assessment methodology was approved by the Board of Directors and management.

VaR - Value at Risk model is a statistical model that estimates the expected loss for the Bank, based on a historical simulation, in the course of a certain investment horizon and on a predetermined statistical level of assurance. The VaR may rise as the result of an increase in the volatility of the risk factors, or as the result of an increase in the inherent risk level of the banking activity. However, VaR is limited in its capability to forecast extreme scenarios and is therefore used as a risk measure mainly in ongoing management, but may also generate a warning sign in extreme market scenarios.

The assessment of risk using VaR is adjusted to the nature of a portfolio's activity and composition - for the trading portfolio, it is calculated with a holding horizon of ten business days, and in the banking portfolio - with a holding horizon of one month, both at a significance level of 99%. In addition, a backtest process is performed regularly, in order to examine the model's validity.

Since the VaR may increase as the result of market volatility, and not necessarily as the result of a change in the risk profile, the Bank has set attention limits, at the Board level, on the VaRs of the banking and trading portfolios. These limits are designed to serve as a warning sign for the risk level which, if reached, requires a reassessment of the risk profile and decisions regarding risk mitigation or temporarily readjusting the limit.

Following is the trading portfolio VaR at the Group level, according to the historical simulation:

	Trading portfolio VaR	
	December 31	
	2017	2016*
	in NIS millions	
Actual	**8**	28

* The data for 2016 were restated.

Sensitivity analyses and stress scenarios - The global and local markets are subject to periodic turmoil, reflected in an exceptionally high parameter volatility, deviating from normal historic behavior. Quantitative models such as VaR do not provide information on losses that may occur in extreme market conditions or beyond the set level of significance. As a result, to detect a change in any of the risk factors, risk is assessed using a variety of extreme market scenarios as well as sensitivity analyses. These include all of the risk factors to which the Bank is exposed and constitute part of the decision-making process for determining the overall investment strategy and preferred composition of the portfolio under the predetermined risk appetite restrictions. In calculating stress scenarios, expert assumptions are validated, as far as possible, against historic data as well as current market data.

Table 32 - Capital requirements for market risks (Pillar 3)

The following table outlines the regulatory capital requirements in respect of exposure to market risks under the standardized approach, which covers only some of market risk exposures.

	December 31	
	2017	2016
	in NIS millions	
Capital requirements [(a)] in respect of:		
Interest rate risk	**478**	478
Share price risk	**20**	44
Foreign exchange rate risk	**95**	70
Options	**21**	19
Total capital requirements for market risks	**614**	611

(a) According to 13.75% and 12.74%, in accordance with the minimum total capital required as at December 31 2017.

Additional information regarding the interest rate risk

The interest rate risk is the risk of loss as the result of changes in risk-free interest rates in various currencies, arising from several sources, such as: gaps between repayment or interest change dates (the earliest of the two) of the assets and liabilities in each of the linkage segments and the basis spread risk.

The interest exposure policy is to limit the effect of potential changes in interest rates on the potential erosion of economic value and the financing profit for the upcoming year.

In reality, the interest rate risk is measured and managed on the basis of various behavioral assumptions as to the repayment dates of the assets and liabilities. According to past experience, the Bank treats some of the current account balances as long-term liabilities. In addition, there are assumptions referring to prepayments of mortgages, on the basis of a statistical model that attempts to forecast prepayments based on interest rates. These estimates are of great importance in managing interest rate risks, inter alia due to the significant increase in these balances in recent years.

The exposure to interest rate changes is measured for both increases and decreases in interest rates in each linkage segment. The measurement is designed to test the sensitivity of the current structure of the value of assets and liabilities to a change in interest rates, and therefore the calculation is performed without changing the asset and liability structure.

Table 33 - Summary of exposures to unexpected changes in interest rates at the Group Level (before tax)*

	The potential change in economic value as a result of a/an:					
	December 31 2017			December 31 2016		
Scenario	Increase of 1%	Decrease of 1%	Increase of 0.1%	Increase of 1%	Decrease of 1%	Increase of 0.1%
	in NIS millions					
in NIS						
Banking portfolio	**(411)**	**306**	**(41)**	(12)	(227)	10
Trading portfolio	**(38)**	**25**	**(3)**	37	(45)	4
In foreign currency						
Banking portfolio	**175**	**(249)**	**22**	(42)	(143)	-
Trading portfolio	**32**	**47**	**2**	52	(49)	5
	The potential change in the annual net income from a					
	December 31 2017			December 31 2016		
	in NIS	Foreign		in NIS	Foreign	
Total	**417**	**391**		523	215	

* The exposure to a 1% interest rate decrease is based on the interest rate on credit and deposits being reduced by the same rate. Since currently, the interest rate on most deposits is less than 1%, and there is a low probability that the interest on deposits will fall below 0%, the above exposure calculation should be considered a measure in line with the accepted standards.

** A decrease in interest rate is expected for lead to a loss of a similar amount.

Table 34 - Capital exposure to an immediate increase or decrease in interest rates (before tax)

	Exposure in NIS			Exposure in foreign		
	As at December 31					
	To an increase of 1%	To a decrease of 1%	To an increase of 0.1%	To an increase of 1%	To a decrease of 1%	To an increase of 0.1%
	in NIS millions					
Capital exposure to an immediate increase or decrease in interest rates*	**1,615**	**(2,083)**	**180**	**(349)**	**352**	**(34)**
	As at December 31 2016					
	To an increase of 1%	To a decrease of 1%	To an increase of 0.1% decrease	To an increase of 1%	To a decrease of 1%	To an increase of 0.1% decrease
	in NIS millions					
Capital exposure to an immediate increase or decrease in interest rates*	1,537	(1,978)	176	(435)	268	(40)

* The measurement includes exposure to an immediate change in the interest rate of the Bank's own portfolios, revalued according to market value and the actuarial obligation for employees. The measurement does not include the sensitivity effect of the plan assets to changes in interest rates estimated - as at December 31 2017 - to be a NIS 134 million decrease in the value of the assets (on December 31 2016 - NIS 117 million) under a scenario of a 1% interest rate increase. Neither does the measurement include the effects of the transitional provisions of the Employee Rights Standard, on which the capital adequacy ratio calculation is based.

During 2017, the Group complied with all interest exposure restriction set by the Board of Directors.

The following are the main restrictions on exposure to market risks as at December 31 2017:

Restriction	in NIS
Sensitivity of the economic value to concurrent interest rate changes of 1%	
The banking portfolio in NIS	**900**
The banking portfolio in foreign currency	**300**
The trading portfolio in NIS	**300**
The trading portfolio in foreign currency	**200**
VaR red flags	
Banking portfolio	**700**
Trading portfolio	**250**

Additional information regarding investment in shares and funds

The Bank has defined the Group's investment policy, including restrictions both on the overall investment amount and the amount per company, the investment mix and the different risk levels for various types of investments.

The Bank's own equity investments are made through investments in indices or tradable investment instruments.

In addition, the Bank has a non-banking investment portfolio, managed by its subsidiary Leumi Partners.

Table 35 - Exposure of the share and fund investments in the banking portfolio (Pillar 3)

	Balance sheet balance and fair value	
	As at December 31	
	2017	2016
	in NIS millions	
Non-tradable shares in the available-for-sale portfolio	**991**	981
Tradable shares and funds in the available-for-sale portfolio	**1,936**	961
Total	**2,927**	1,942

Liquidity risk

Liquidity risk is the risk arising due to uncertainty regarding the possibility of raising sources and/or disposing of assets, unexpectedly and within a very short time, without incurring a substantial loss. The Leumi Group's liquidity risk management policy is part and parcel of its strategic business management and is adapted to the requirements of Proper Conduct of Banking Business Directive No. 342, *Liquidity Risk Management,* and the requirements of Proper Banking Management Directive No. 221, *Liquidity Coverage Ratio*, which adopts the recommendations of the Basel III Committee for calculating the liquidity coverage ratio (LCR), with adjustments for the Israeli economy.

Proper Conduct of Banking Business Directive No. 221, *Liquidity Coverage Ratio*, stipulates that a bank shall have a sufficient inventory of high-quality liquid assets to meet the liquidity requirements for a time-horizon of 30 days, under a combined stress scenario presented in the Directive.

The Directive prescribes the manner of calculating the liquidity coverage ratio, including the characteristics and operational requirements for an "inventory of high-quality liquid assets" and sufficient buffers for them (the numerator); it also prescribes the net cash outflow expected under the stress scenario defined in the Directive for the next 30 calendar days (the denominator). The cash flow includes, inter alia, withdrawal of deposits of various types according to coefficients set forth in the Directive, utilization of credit facilities extended by the Bank, etc. less repayments of loans granted by the Bank, during the month, according to the cash inflow coefficients specified by the Directive. As a result, changes in the volume or composition of liquid assets, changes in the amount of deposits of each type defined by the Directive, changes in the volume of credit facilities and their collateral for which liquidity is to be maintained, etc., could lead to a change in the Bank's liquidity coverage ratio.

As of January 1 2017, the minimum liquidity coverage ratio for the Bank and the Group is 100%.

In addition to measuring the minimum liquidity coverage ratio, the Bank manages an internal model for estimating liquidity risk under a variety of scenarios relating to various market situations which pertain to the entire banking system and to Leumi in particular. The scenarios ensure that the liquid sources available to the Bank in all currencies, and separately in foreign currencies, provide sufficient liquidity to meet all of its liquidity requirements for up to 30 days. The model is based on an assessment of the quality and diversification of the asset portfolio, using adequate safety cushions that were tested historically according to the risk levels, the scenario narrative and based on the opinion of professional entities. The model also estimates the stability of deposits by the public according to customer characteristics. The restrictions for the internal model were set at several levels of management, primarily by the Board of Directors. During the period under review, the Bank's liquidity ratio was above 100%.

The liquidity risk management policy

Leumi maintains a proper liquidity level by investing its own portfolio in high-quality and diversified assets in NIS and foreign currencies, to enable it to meet all liquidity needs under a variety of stress scenarios, as well as through a policy of raising diversified and solid sources with different time ranges and emphasis on raising deposits from retailers and issuing long duration debentures.

The management of exposure to liquidity risks is regularly examined, controlled and discussed by the forums and committees at the Board of Directors, management and intermediate levels. In this framework, ongoing follow-up is conducted on cash flow forecasts, trends in various deposit segments, concentration of depositors and fund raising costs. The exposure to liquidity risks is regularly managed at the Group level and a group monitoring process is being developed. The subsidiaries establish liquidity risk management policies and manage the liquidity ratio independently, in line with the Group's policy and subject to the local regulatory framework applicable to each company. Furthermore, the Group set credit lines for the subsidiaries, which were approved by the Board of Directors, in case of a stress scenario that requires injecting funds to the subsidiaries, subject to regulatory restrictions for transferring funds.

The management of foreign currency liquidity is also affected by activities in NIS and foreign-currency derivatives, which may create currency fluctuations in the liquidity measures, and are therefore closely monitored and managed.

Table 36 - Liquidity coverage ratio (Pillar 3)

	For the three months ended December 31			
	2017		2016	
	(Average) total unweighted value[(a)(d)]	(Average) total weighted value[(b)]	(Average) total unweighted value[(a)(d)]	(Average) total weighted value[(b)]
	in NIS millions			
Total high-quality liquid assets	**-**	**113,298**	-	109,432
Cash outflows				
Retail deposits from individuals and small businesses, of which:	**174,315**	**12,227**	175,501	11,670
Stable deposits	**45,061**	**2,253**	46,805	2,340
Less stable deposits	**69,571**	**8,184**	62,805	7,353
Deposits for a period exceeding 30 days (Section 84)	**59,683**	**1,790**	65,891	1,977
Unsecured wholesale financing, of which:	**141.073**	**93,293**	129,542	82,065
Deposits for operational needs and in chains of cooperative banking corporations	**-**	**-**	-	-
Non-operational deposits (all counterparties)	**140,776**	**92,996**	129,108	81,631
Unsecured debts	**297**	**297**	434	434
Secured wholesale financing	**-**	**-**	-	-
Additional liquidity requirements, of which:	**70.162**	**9,516**	82,043	20,017
Cash flows from derivatives and other security requirements	**4,091**	**4,091**	14,694	14,694
Cash flows from loss of debt product financing	**-**	**-**	-	-
Credit lines & liquidity	**66,071**	**5,425**	67,349	5,323
Other contractual financing commitments	**6,049**	**6,049**	6,317	6,317
Other contingent financing commitments	**41,055**	**1,330**	43,060	1,474
Total cash outflows	**-**	**122,415**	-	121,543
Cash inflows				
Secured loans (e.g., transactions to resell)	**1,346**	**-**	1,358	-
Cash inflows from regularly repaid exposures	**41,119**	**27,538**	40,960	26,853
Other cash inflows	**8,817**	**2,120**	17,532	11,992
Total cash inflows	**51,282**	**29,658**	59,850	38,845
Total adjusted value[(c)]	**-**	**-**	-	-
Total high-quality liquid assets	**-**	**113,298**	-	109,432
Total cash outflows, net	**-**	**92,757**	-	82,698
Liquidity coverage ratio	**-**	**122%**	**-**	132%

(a) Unweighted values are calculated as outstanding balances due or repayable by the holder within 30 days (for cash inflows and outflows).
(b) Weighted values are calculated after applying appropriate safety cushions or inflow and outflow rates (for cash inflows and outflows).
(c) Adjusted values will be calculated after activating (1) safety cushions and cash inflow and outflow rates; and (2) all relevant restrictions (i.e., restriction on high quality liquid assets at Tier 2b and Tier 2 and a restriction on inflows).
(d) The values are calculated at the bank level, based on an average of 77 daily observations during Q4 2017 (70 observations during Q4 2016).

In the past year, the liquidity coverage ratio declined, mainly in Q2 2017, due to the repayment of subordinated capital notes financed by raising highly attractive business deposits.

Table 37 - Composition of high-quality liquid assets by average balance per quarter

	For the three months ended December 31					
	2017			2016		
	In NIS	In foreign currency	In NIS and foreign currency	In NIS	In foreign currency	In NIS and foreign currency
	Total weighted value in NIS millions					
Total Tier 1 assets	**86,328**	**23,562**	**109,890**	81,645	25,330	106,975
Total Tier 2A assets	**-**	**3,153**	**3,153**	-	2,224	2,224
Total Tier 2B assets	**45**	**210**	**255**	93	140	233
Total high-quality liquid assets	**86,373**	**26,925**	**113,298**	81,738	27,694	109,432

The models serve as a dynamic management tool, allowing ongoing daily oversight, supervision and control of the liquidity status, and their results are reported to all the relevant management and control parties. In addition, exposures are reported in the CEO's Report and in the quarterly risk paper discussed by management, the Risk Management Committee of the Board of Directors and the Board of Directors plenum.

The Bank has a contingency plan in place for handling a liquidity crisis, which includes a system of warning signs that may indicate a shift in the Bank's liquidity position. On the appearance of warning signs, a special forum will convene to assess the situation and examine the need to activate the plan, based on the level of severity. The plan includes detailed operational measures outlining, among other things, the order of asset disposal, customer care policies, and systems of reporting to all business entities, the Board of Directors and the Bank of Israel.

Financing risk

Financing risk is the risk of an insufficiently stable financing source structure which fails to serve its designated uses in the long term.

Over the years, the Bank has managed an extensive and diversified infrastructure of stable financing sources for various time periods. The Bank's main source of financing is deposits from retail customers. In addition, the Bank finances its activity through deposits made by commercial and business customers and by issuing notes payable. The sources are managed on an ongoing basis, separately for NIS and foreign currencies. The sources are invested in credit and liquid assets, mainly low-risk debentures and short-term swaps. The Bank has a wide range of foreign currency sources from local retail, business and financial customers, as well as from foreign residents.

The concentration of financing sources is managed and monitored using risk management indicators and models. The Bank performs follow-up on the composition and concentration of sources by several categories: customer size and type, single depositor, deposit's life, typical behavior over time. The ongoing management of the sources' composition includes developing a policy for source diversification and financing periods. The concentration of the sources is controlled and managed by the Bank as part of its liquidity risk management. Ongoing daily measurement of the liquidity indicators, minimum coverage ratio, and monitoring of warning signs enable dynamic management and follow up to ensure that the sources are sufficiently diversified, and that the liquidity status and trends are adequately supervised and controlled.

Table 38 - Pledged assets by balance sheet line item (EDTF)

	December 31 2017			
	Pledged assets related to			
	Deposits collateral	Clearing house and risk fund activities	CSA agreements	Derivative activities
	in NIS millions			
Cash and deposits with banks	**-**	**-**	**495**	**1,289**
Securities	**4,178**	**930**	**-**	**2,015**
Loans to the public	**-**	**80**	**1,764**	**-**

	December 31 2016			
	Pledged assets related to			
	Deposits collateral	Clearing house and risk fund activities	CSA agreements	Derivative activities
	in NIS millions			
Cash and deposits with banks	-	-	484	121
Securities	2,698	911	-	1,267
Loans to the public	-	69	1,190	-

Operational risks

Operational risk is the risk of loss as a result of inadequate, or failure of, internal processes, people and systems, or external events.

The Leumi Group engages in a wide range of financial activities and is therefore exposed to operational risks which include, inter alia: information security and cybersecurity risks, technological risk, business continuity risk as well as embezzlement and fraud risks.

The Group's operational risk is managed through its three lines of defense and involves an ongoing proactive process to identify, assess, measure, control, minimize, monitor and report the material risks performed by all divisions.

The operational risk management organizational structure

First line of defense - The business lines' managements, support units and Leumi Technologies are responsible for managing the operational risks in their respective purviews, both on an ongoing basis and for new projects and products.

Second line of defense - the Operational, IT and Cybersecurity Risk Department in the Risk Management Division is responsible for, and leads, the operational risk management process, while developing policies and methodologies and exercising professional responsibility. The Division is professionally in charge of guiding and challenging (subject to materiality) the first line of defense in the risk management process - both on an ongoing basis and for material new projects and products.

Third line of defense - Internal Audit. The Internal Audit Division is an independent unit responsible for examining whether the risk management processes are in line with the Bank's targets and exposing any internal control vulnerabilities.

Management and board of directors' committees - Each quarter, the committees hold a discussion on the material exposures to operational risks. The operational risk management policy is brought before the Board of Directors for discussion and approval.

The operational risk policy and management framework

The Group's operational risk management policy outlines Leumi's operational risk management principles, guidelines and approach, including: risk-oriented management adapted to each business line and a focus on risks with potentially significant consequences.

To allow the Board of Directors and management to exercise appropriate corporate governance, operational risk tolerance was defined as quantitative restrictions and qualitative declarations.

The operating risk profile is periodically monitored and reported on a quarterly basis to the Bank's management and Board of Directors, serving as a basis for decision-making.

The Bank revises the operational risk map on an ongoing basis. The revision is made by the first line units, with the Risk Management Division providing guidance, challenging, and assistance. The process includes identification and (qualitative and quantitative) assessment of the risks and recommendations for minimizing the risks (risk mitigation plans). In addition, there is a system in place supporting risk reporting, implementation and documentation of controls, mitigation plans and failure events.

The Bank manages risks in material new projects and products on the basis of a methodology which includes risk identification and mitigation with the aim of complying with Leumi's business and operating goals.

Since the operational risks are cross-organizational, the Risk Management Division is taking steps to instill an advanced operational risk management culture, including reporting on incidents and drawing conclusions.

The regulatory capital in respect of operational risk is calculated using the Basel standardized approach.

To minimize potential damage in the event of risks materializing, the Leumi Group has purchased a variety of insurance policies covering various operational risk, including, inter alia, a cybersecurity policy and banking insurance policy.

Main operational risk areas

Information security and cybersecurity risks

The shift to digital banking and the information revolution have led to the adoption of new technologies and products, including cloud products, which constitute significant means to achieving the business targets. The multiple systems and interfaces and the growing dependence on technology increases the exposure to information security and cybersecurity threats and risks.

Cyberspace is highly dynamic in terms of the type, scope and force of the attacks. These risks may expose the Bank to business and reputational damage.

The information security cybersecurity strategy and policy are updated in line with the continuous changes in the business-financial environment and threat map. The information security and cybersecurity approach focuses the allocation of security resources differentially, according to the risk level, taking into account technological, business, human and physical aspects.

Sensitive data are protected on several levels: the databases, IT systems, access permissions to the systems and their day-to-day management, through physical security means and by increasing awareness among all employees.

In 2017, due to constant changes in the financial business environment and the cyberspace threat map, Leumi developed a cybersecurity policy that reflects an integrative holistic approach to coping with cybersecurity threats and incorporates the cybersecurity strategy and cybersecurity risk management framework. The policy also includes an approach to monitoring and handling possible cybersecurity threats.

In 2017, no cybersecurity incidents or embezzlements were discovered which affected the Bank's financial statements.

Technological risk

Bank Leumi champions and initiates technological innovation. To offer its customers advanced services, the Bank requires advanced digital infrastructures which, on the one hand, create business opportunities, while on the other hand, raise its level of exposure to technology risks in the business and operating processes. The IT environment is complex, ever changing and organizations are becoming increasingly dependent on it.

The Bank attributes great significance to having a stable, durable and robust technology infrastructure. As a result, the Bank invests resources in reducing the number of technological failures and minimizing the potential damage to the business and operational activities.

Leumi also contracts suppliers and subcontractors to develop new products and for ongoing operational purposes. Its dependence on the suppliers exposes the Bank to business continuity issues, which may lead to disruptions and information leaks. Such risks are managed on an ongoing basis through the procurement, information security and cybersecurity workflows.

During October 2017, the scoping stage of the core system replacement project began, during which the project's scope, resources, schedule and complexity will be evaluated.

Business continuity risk

The Bank manages and implements business continuity processes, in which it prepares to recover from disaster events and maintain its business continuity. The processes include the following:

- A business continuity policy that defines corporate governance, principles, and the key processes in case of an emergency.
- A work framework that includes business continuity plans, business impact analysis, recovery strategies and a drill methodology.
- Technological infrastructures - the Bank's computer array is comprised of two computing centers and additional backup center.

Embezzlement and fraud

The digital workplace environment increases the intensity of embezzlement and fraud risks in terms of identity, money and information theft as well as customer information leaks and misuse of information.
Leumi invests significant resources in identifying and mitigating these risks through focused, ongoing monitoring.

Other risks

Regulation and compliance risks

Regulation risk

In the past few years, capital and liquidity requirements from banks – both in Israel and around the world – have been significantly extended, following the lessons drawn from the financial crisis (Basel III Rules). In addition, international guidelines regarding new standards which were issued lately may affect the Bank's capital and risk-weighted assets. These trends affect the capital allocation for the Group's various business activities. In addition, laws and regulations were recently published which focus on the consumer environment and which aim, among other things, to increase competition.

The increase in regulatory requirements in Israel and abroad affects the Group's business model, profitability and capital adequacy requirements.
The Bank monitors these developments, studies them and prepares accordingly.

Compliance risk

a. Compliance risk, prohibition oמ money laundering and financing of terrorism

To effectively manage compliance risk, Leumi has in place a compliance and enforcement array, headed by the Chief Compliance Officer. The latter is responsible, among other things, for meeting the legal requirements of the prohibition on money laundering and financing of terrorism. The Chief Compliance Officer also serves as the securities law enforcement officer and the responsible officer for FATCA.

The activity of the Compliance Department is performed by a professional team with extensive knowledge and understanding in the field of compliance, and is based on work processes, risk-based controls and automated systems.

The Compliance and Enforcement Department reports to the Chief Legal Counsel.

The complexity of and developments in banking activity requires the Bank to strictly comply with all applicable requirements in its relations with customers, under primary legislation, regulations, ordinances, permits and the Bank of Israel's directives, as well as global regulations and standards governing the Bank's activities.

Proper Conduct of Banking Business Directive No. 308, *Compliance and the Compliance Function in Banking Corporations*, formally defines the compliance function's areas of responsibility at the Group level. The directive outlines the definition of compliance provisions and stipulates that compliance risk stems from laws, regulations, directives, internal procedures, conduct rules and Israel Security Authority's position papers. The directive stipulates that a bank must assess the effectiveness of its compliance risk management, and find means to measure it, with the compliance risk derived, as stated above, from the entire body of laws governing the Bank's activity.

The directive provides that the compliance function shall be responsible at least for the compliance risk derived from the core regulations (such as those covering a bank's conduct towards its customers, money laundering and the financing of terrorism, advice to customers, conflicts of interest, privacy protection, taxation aspects relevant to products or services provided to customers, etc.). Insofar as the risk is derived from other provisions applicable to a banking corporation, the latter may be managed by other functions from the second line of defense.

Pursuant to the directive, a comprehensive compliance policy paper is revised and approved by the Board of Directors each year. The policy paper includes corporate governance issues such as the purviews of and Board of Directors, management and Chief Compliance Officer, and the three defense lines' respective areas of responsibility.

A new methodology was established for assessing risk embodied in regulatory directives (compliance directives as defined by the new directive). Pursuant to the directive, the Compliance Department prepares a multi-year risk-oriented work plan, including a schedule for tasks and activities.

Maintaining a fair compliance culture across the entire organization requires an effective control and enforcement framework, which is outlined in work processes and enables the organization to comply with all regulations. To this end, strict compliance and enforcement processes have been established for all workflows and their compliance risks. The purpose of the control and enforcement framework is, among other things, to identify existing and potential gaps and exposures in order to determine whether work processes, procedures, training program and assimilation requirements need revision. The control processes are based, inter alia, on an analysis of the compliance regulations, internal and external audit findings, complaints by the public, legal proceedings against the Bank or other banks that may indicate possible compliance exposures, as well as analysis of trends and events in Israel and around the world.

The Department is in regular contact with subsidiaries in Israel and abroad, for the purpose of monitoring the implementation of compliance issues as a whole and implementation of the collective compliance policy.

Pursuant to the developing trends around the world, the Bank handles a range of compliance issues, including the prohibition on money laundering and on the financing of terrorism and taxation aspects. Among other things, the Bank focuses on risk areas in financial technology domains (such as FinTech, P2P, hedge funds, virtual currencies, etc.) – managing compliance risk and prohibition on money laundering risk in a developing financial technology environment characterized by a lack of well-defined and highly experienced regulation on the one hand, and on the other hand – by professional complexity and the lack of practices incorporated into the control processes due to the novelty of the issues at hand.

b. Administrative enforcement

In January 2011, the Law of Efficiency of Enforcement Procedures in the Israel Securities Authority (Legislative Amendments), 2011 was passed into law by the Knesset. The aim of the law is to improve the enforcement efficiency in the field of securities laws. The law allows to impose various sanctions on a corporation which has violated relevant provisions, including its officers and employees. Further to the law, the Israel Securities Authority published a list of criteria for recognition of an internal securities and investment management enforcement program (hereinafter: the "Criteria List").

The Criteria List instructs corporations to appoint an enforcement officer. His function, according to the Criteria List, is to be responsible for implementing the enforcement program.

The Group's Chief Compliance Officer also serves as enforcement officer. The Board of Directors has approved the internal enforcement plan, after the plan had been validated by an outside specialist, who had also reviewed the main enforcement procedures.

c. FATCA - Foreign Account Tax Compliance Act

According to Amendment 227 to the Income Tax Authority and Income Tax Regulations (Implementation of the FATCA Agreement), 2016, the Bank is required to identify customers and forward information on accounts held by U.S. customers to the Israel Tax Authority, to be forwarded to the US's Internal Revenue Service.

The Bank implements a declared money policy while ensuring that no funds managed by the Bank go undeclared to the relevant tax authorities. In this context, various measures were taken to locate and identify the relevant target audiences, and reports were made to the tax authorities in accordance with the FATCA rules, as agreed between Israel and the US tax agencies.

The Bank acts on several levels to ensure the compliance of Leumi Group and individuals therein with the provisions of the law, including: appointment of a compliance as the party responsible; adoption of appropriate policy and work procedures; development of automated tools supporting the working processes; formulation of training and assimilation, testing, control and operation mechanisms required for complying with the directives and instructing the Group's subsidiaries on adequate preparations.

d. Common Reporting Standard (CRS)

The OECD published a uniform standard for implementing the Automatic Exchange of Information regarding Intergovernmental Financial Accounts (hereinafter: the "Standard"). The standard is formulated in the spirit of the US FATCA and is intended to increase transparency and supervision over tax reporting by residents of the countries holding financial accounts outside their countries of residence. In July 2016, Amendment 227 to the Income Tax Ordinance was published, regarding the implementation of the FATCA and the Standard. Regulations for applying the Standard have not yet been published.

Leumi is prepared for complying with the legislative requirements. The branches of Bank Leumi in the UK and Romania have begun to implement the Standard on January 1 2016, in accordance with the local applicable regulatory directives.

e. Subsidiaries and foreign offices

According to the Bank's policy, compliance risk is managed at the Group level. In this context, various steps are taken to supervise and control and foreign offices and subsidiaries in order to monitor compliance issues as a whole and apply the Group's compliance policy.

Legal risk

Legal risk is defined as the risk of loss as a result of inability to legally enforce an agreement or contingent liabilities, including in respect of claims against, and demands from, the Bank. The definition includes risks arising from legislation, regulations, court rulings and directives issued by authorities, risk emanating from activity that is not covered by adequate agreements, without legal advice or under faulty legal advice, as well as a result of interpretation of the rights of parties to agreements between the Bank and its customers.

Legal risk arises from five main areas:

- Legislation risk - risk attributable to the Bank's activity which does not comply with a primary or secondary legal provision, a Bank of Israel directive or a directive issued by other competent authorities.
- Contractual risk - risk attributable to the Bank's activity with customers, suppliers and other parties with whom the Bank contracts, if it is not backed by an agreement that fully establishes the Bank's interests, or the agreement is not fully enforceable or includes illegal terms and conditions.
- Court ruling risk – risk arising from the Bank's activity if it does not comply with case law.
- Risk attributable to legal proceedings conducted against the Bank.
- Risk arising from changes in enforcement policy.

Legal risk policy and management framework

The Chief Legal Counsel, who is a member of the Bank's management and Head of the Legal Division, is responsible for leading legal risk management.

The Group implements a program for managing legal risk, which aims to identify, prevent, manage and mitigate legal risk. The program includes policy papers and an interface between the Legal Counsel 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 within the Bank is professional and up-to-date. The policy document has been revised periodically over the years, including in 2017.

The Group drew up a general policy paper, applicable to all subsidiaries, for managing legal risk, according to which each company prepared an internal procedure for managing legal risk in line with its activity and the Group's policy. The internal procedures have been approved by the Legal Division and by the subsidiaries' board of directors. According to the policy papers, the subsidiaries are required to seek adequate legal advice for certain issues. In addition, the companies send periodic and immediate reports to the Legal Risk Officer, as required by the policy paper. The reports were sent in a uniform format prepared by the Legal Counsel Division. In 2017, the legal risk management policy papers of the foreign subsidiaries were revised. A legal stress scenario was updated as well.

In the context of the legal risk management program, the following points have been emphasized:

- Preventing and mitigating legal risk.
- Identifying and handling sources of material legal risk.
- Preparing adequate agreements, guidelines and procedures.
- Reviewing statutory provisions (including case law) and regulatory directives, and their implications for the Bank
- Drawing conclusions on various topics and implementing the conclusions drawn in legal documents used by the Bank, as well as providing opinions on these topics to the relevant units in the Bank.

The parties responsible for executing the legal risk management program include various officials and committees within the Legal Counsel Division, headed by the Chief Legal Counsel - who also serves as Legal Risk Officer - whose function is to review, coordinate and handle new legislation and rulings applicable to the Bank.

The Regulation Unit in the Strategy and Regulation Department is engaged in identifying and, if necessary, handling new regulations (primary legislation, secondary legislation, directives issued by authorities), as early as the proposed law or regulation stage.

The activity of each of the abovementioned officials and committees is prescribed by internal work procedures of the Legal Counsel Division. The procedures stipulate, inter alia, the information interfaces between the various parties and the Division's management and legal risk team.

General legal exposure

There is general exposure, which cannot be assessed or quantified, arising, inter alia, from the complexity of the services provided by the Bank and the consolidated companies to their customers. The complexity of these services embodies, inter alia, a potential for claims, interpretations and others, relating to several commercial and regulatory terms and conditions. It is impossible to foresee all of the types of claims which may be raised in this area and the exposure deriving from these and other claims in connection with the services provided by the Bank and the consolidated companies, which are filed, inter alia, via the procedural mechanism provided in the Class Action Law.

There is also exposure due to regulatory changes and directives issued by the Banking Supervision Department, the Israel Securities Authority and other regulators to which the Bank is subjected. Some engagements with customers last many years, in the course of which policies, regulations and legal trends, as well as court rulings, may change. The Bank and the consolidated companies use complex automated systems, which are adjusted on a regular basis in light of the changes as aforesaid. All these create an increased operating and legal exposure.

There is also a general exposure arising from complaints filed from time to time with the Banking Supervision Department against the Bank and the consolidated companies, which may, under certain circumstances, result in legal proceedings against the Bank. Currently, it is impossible to assess whether there is exposure in respect of such complaints and whether the Banking Supervision Department will issue an industry-wide decision about the complaints and/or whether class actions or other type of lawsuits will be brought as a result of such proceedings. It is therefore impossible to assess the potential exposure for the such complaints. Accordingly, no provision was included in respect of the said exposure.

Reputational risk

Reputational risk is the risk of damage to the confidence of one of the Bank’s various stakeholder groups (customers, shareholders, employees, etc.) in light of the publication or public disclosure of a transaction or practice, business results or other events relating to the Group.

The Bank possesses functions that handle reputational risk management, the purpose of which is to identify, manage and mitigate the risk.

Strategic risk

Strategic risk is defined as the risk of a material decline in profitability arising from a decrease in income which cannot be compensated for through a sufficient reduction in expenses or by finding other sources of income. Such a decline may result from erroneous strategic decisions, an inability to implement adequate strategies, inadequate implementation of decisions or lack of response to or preparation for changes in the business environment (industry-specific, economic, regulatory, consumer-related or technological).

Strategic risk may be one whose damage affects the Bank’s business model or one of its material business lines. This type of risk may have an effect on profit that is insignificant in the immediate term, but which may become dramatic in the long term.

Strategic risk management involves several functions: The Strategy and Regulation Division, the Risk Management Division and the Finance Division. These functions are in charge of identifying, mapping, assessing and monitoring this risk for all of the Bank’s units, including the business lines, management and the Board of Directors.

For more information on the severity of the risk factors, please see under “Exposure to Risk and Methods of Risk Management” in the Report of the Board of Directors and Management.

Leading and emerging risks

In recent years, leading risks arise from the Bank's operating environment, which has been highly affected by risks related to regulation and legislation, a volatile macro-economic environment, and changes in the business model - including the transition to digital "new banking" and new social and consumer trends. Emerging risks are ones whose characteristics and severity vary according to the changes that have occurred in recent years in the competitive, consumer, regulatory and technological environments. These include cybersecurity, technological, and conduct risks.

The following are the key risks expected to affect the Bank:

Macroeconomic risk

Macroeconomic risk is the risk to the Group's income and capital arising from macroeconomic conditions, including a low interest rate environment, global political power relations and their impact on global trade – the US's economic policy, social and political processes in Europe and geopolitical instability in conflict zones around the world, inter alia on the back of the increased threat of terrorism.

The Bank is assessing its ability to withstand negative developments in the microeconomic environment using systemic stress scenarios. In addition, ongoing monitoring and follow up of market developments are conducted in order to prepare in advance and adapt the activity, as needed.

Regulation risk

In the past few years, capital and liquidity requirements from banks – both in Israel and around the world – have been significantly extended, following the lessons drawn from the financial crisis (Basel III Rules). In addition, international guidelines regarding new standards which were issued lately may affect the Bank's capital and risk-weighted assets. These trends affect the capital allocation for the Group's various business activities.

In addition, laws and regulations were recently published which focus on the consumer environment and which aim, among other things, to increase competition.

The increase in regulatory requirements in Israel and abroad affects the Group's business model, profitability and capital adequacy requirements. The Bank monitors these developments, studies them and prepares accordingly.

Information security and cybersecurity risks

The quick developments in cyberspace have led to an increase in the scope and force of the threats, the perpetrators' capabilities and the complexity of the attacks and, as a result, in a significant increase in the exposure to the cybersecurity risk. These risks may expose the Bank to business and reputational damage.

In 2017, as part of its effort to boost its cybersecurity defenses and manage the cybersecurity risk, Leumi developed a cybersecurity policy that reflects an integrative holistic approach to coping with cybersecurity threats and incorporates the cybersecurity strategy and cybersecurity risk management framework. The policy also includes an approach to monitoring and handling possible cybersecurity threats.

For more information, please see under "Operational risk".

Technological risk

Bank Leumi champions and initiates technological innovation. To offer its customers advanced services, the Bank requires advanced digital infrastructures which, on the one hand, create business opportunities, while on the other hand, raise its level of exposure to technology risks in the business and operating processes. The IT environment is complex, ever changing and organizations are becoming increasingly dependent on it.

The Bank attributes great significance to having a stable, durable and robust technology infrastructure. As a result, the Bank invests resources in reducing the number of technological failures and minimizing the potential damage to the business and operational activities.

For more information, please see under "Operational risk".

Conduct risk

Conduct risk is the risk that the Bank's conduct vis-à-vis its customers will lead, by act or omission, to an unwanted outcome for them, without the customer being able to take that outcome into account. As a result, the Bank may incur losses from legal damages, fines or reputational damage.

Bank Leumi adheres to transparent and fair practices in an effort to provide its customers with valuable services and products. This principle is reflected in the Bank's vision – to champion proactive, high-quality banking for its customers. In addition, the proactive and sale processes are subject to procedures and controls which ensure proper conduct. These processes are assessed on a regular basis, with the aim of continuously upgrading them.

During the reporting year, the Bank developed and approved a policy for managing conduct risk vis-à-vis the Bank's retail customers

Remuneration

Below is the Bank's disclosure on remuneration, pursuant to the disclosure requirements under Pillar 3 of the Basel Accord, as stipulated in the Supervisor of Banks' Reporting to the Public Directives.

For more information, please see Note 23 to the 2017 financial statements. For more information regarding officeholder and interested party remuneration, please see under "Remuneration of Senior Officeholders" in the Bank's Corporate Governance Report for 2017.

Qualitative disclosure

a. Information about the functions supervising remuneration

Name, composition and purview of the main function supervising remuneration	The Board of Directors' Remuneration Committee[1] is the primary function supervising remuneration in the Bank. The following are some of the committee's roles: it discusses, approves and provides recommendations to the Board of Directors regarding the Bank's remuneration policy, officeholder employment and the underlying principles of other employees' terms of employment.
Details of external consultants the Bank wishes to consult regarding remuneration, the function requesting the service and in which aspects of the remuneration processes.	Cognum Financial Consulting Ltd. advises the committee on financial matters and Adv. Eyal Dotan of the Meitar Liquornik Geva Leshem Tal law firm provides legal support.
Description of the scope of the Bank's remuneration policy.	The Bank's officeholder remuneration policy includes three policy papers: a remuneration policy applicable to the Bank's officeholders; a remuneration policy applicable to key employees (who are not officeholders); and a remuneration policy for the Bank's other employees. The remuneration policy applies to the entire group, with the subsidiaries using it as recommended guidelines for their own remuneration practices. The remuneration policies for the Bank's officers and key employees are for October 2016 to the end of 2019.
A description of the types of employees defined as officeholders and other key employees, including the number of employees in each group.	The Bank's officeholder group comprises the Board's thirteen directors (including the Chairman of the Board), the President & CEO and the fourteen members of management (including the Chief Internal Auditor) as well as two officeholders who are not members of management. The Bank's other key employees[2] include approximately one hundred persons.

b. Information on planning and structure of remuneration processes

Review of the main characteristics and the remuneration policy objectives	The remuneration policy is based, inter alia, on the provisions of Amendment 20 to the Companies Law, on Proper Conduct of Banking Business Directive No. 301A regarding the remuneration policy in a banking corporation and on the Law of Officeholder Remuneration in

1 On December 31 2017, the Bank's Board of Directors decided to merge the Remuneration Committee with the Audit Committee, in accordance with Proper Conduct of Banking Business Directive No. 301 of the Banking Supervision Department.

2 According to the definition of this term in Directive 301A (excluding officeholders).

	Financial Corporations (Special Permit and Non-Tax-Deductible Expenses Due to Exceptional Remuneration), 2016 (hereinafter: the "Remuneration Limitation Law.") The policy includes, inter alia: provisions regarding fixed remuneration, variable remuneration and the conditions for receiving it; terms of termination of employment; terms under which the Bank may demand a partial refund of bonuses granted; and various provisions intended to prevent taking risks that deviate from the Bank's risk appetite, such as provisions requiring, pursuant and subject to the directive of the Banking Supervision Department, to defer part of the variable bonus.
Review of changes made in the Bank's remuneration policy throughout the reporting year.	No changes were made to the remuneration policy applicable to the Bank's officeholders in 2017. In December 2017, the remuneration policy for key employees (who are not officeholders) and the remuneration policy for all Bank employees was revised, placing special emphasis on compliance aspects.
Discussion of the manner in which the Bank ensures that employees who handle risks and compliance are rewarded independently of the businesses they oversee.	The variable annual remuneration structure under the new remuneration policy ensures that employees who handle risks and compliance are rewarded independently of the businesses they oversee. Thus, a significant part of the total variable annual remuneration is based on personal performance and qualitative criteria in accordance with the relevant officeholder's purview, independently of the business results of the Bank and/or business units overseen by employees engaged in risk management and compliance. In addition, due to the Remuneration Limitation Law, the annual remuneration policy was reduced to a maximum of seven monthly salaries per year, thus no longer requiring differentiation between employees engaged in risk management and compliance and other employees, in terms of the ratio between the variable remuneration and the fixed one.

c. Description of the manner in which existing and future risks are taken into account in the remuneration process

Review of the main risks taken into account by the Bank when applying remuneration indicators.	The purpose of the variable remuneration mechanism in the Bank's remuneration policy is to prevent taking short-term risks. Thus, for example, the measurable variable bonus component outlined in the remuneration policy - which is based on the Bank's return on equity - is calculated according to the Bank's return on equity over a period of three years. In addition, as part of the qualitative variable bonus, failures relating to non-compliance with the Bank's policies and procedures are also taken into account, including deviations from the Bank's risk management policy and/or risk appetite. The remuneration policy also establishes mechanisms aimed at creating incentives to ensure that the remuneration amount is affected by an actual materialization of the risks, such as a mechanism that requires, in certain cases, deferral of part of the variable bonus over several years, provisions enabling partial or full claw-back of all variable bonuses under certain conditions, etc. In addition to the above, following the enactment of the Remuneration Limitation Law, the variable bonus is lower than in the past. In and of itself, this reduction could reduce the incentive to take risks that deviate from the Bank's risk appetite. For more information, please see below.
Review of the nature and type of key indicators used to take into account these risks, including risks that are difficult to measure, and discussion of the manner in which these measures affect remuneration.	The Bank's remuneration policy prescribes various mechanisms to ensure that the various risks related to its activity are taken into account in determining the remuneration of the key employees, including: A limitation on the ratio between the variable remuneration and fixed remuneration key employees may receive, in accordance with Directive 301A; measuring performance to determine the bonus component based on the Bank's return on equity in the last three years. In addition, an upper limit was set for the rate of return on equity for which maximum remuneration is received, in accordance with the Bank's risk appetite; A mechanism to defer part of the variable bonus in accordance with and subject to Directive 301A; the threshold conditions for receiving the measurable variable bonus is the Bank's compliance with the capital adequacy ratios required by the directives of the Banking Supervision Department during the bonus year; The qualitative personal bonus is based, inter alia, on: compliance with the laws and regulations; compliance with the Bank's procedures; no material deviation from the policies set by the Board of Directors, including adherence to the Bank's risk management policy and risk appetite; audit reports covering the key employee; the Board of Directors is authorized to reduce the measurable variable bonus.
Discussion of the manner in which the nature and type of these indicators have changed over the past year and the reasons thereof, as well as the effect of the changes on remuneration.	In 2017, there was no change in the nature and type of these indicators in the Bank's officeholder remuneration policy. In 2017, a change was introduced in the remuneration policy for key employees (who are not officeholders) which further emphasized the weight given to compliance aspects in determining the variable annual remuneration.

d.	Description of the manner in which the Bank links performance to reward levels during the performance measurement period
Review of the Bank's main performance indicators - both for the upper level of the business lines and personal performance.	• The main performance indicators are: The Bank's return on equity over the last three years; the ratio between the annual return on the Bank's stock and the annual return on the Tel Aviv Bank index (excluding the Bank's stock). • Measurement of personal qualitative criteria in accordance with the key employee's purview, such as: implementing and promoting strategic plans and objectives; increasing efficiency; promoting projects; complying with laws and regulations; audit reports; etc.
Discussion of the manner in which personal remuneration is linked to the results of the bank as a whole and to personal performance.	See above.
Discussion of the main indicators used by the Bank to adjust the remuneration in the event that the performance indicators are weak (including the criteria for determining when performance indicators are weak).	Under the remuneration policy, the Bank's key employees are entitled to the measurable annual bonus if the Bank meets the capital adequacy ratios required by the directives of the Supervisor of Banks during the bonus year. In addition, a substantial part of the annual measurable bonus is conditional on the Bank's reaching a minimum of 6% weighted return on equity during the bonus year (calculated over three years, as mentioned above). If the variable remuneration is higher than 40% of the annual fixed remuneration, a mechanism of deferral whereby half (50%) of the amount of the variable remuneration is paid in cash, and the other half is paid in three equal tranches: at the end of the year, after two years and after three years. The deferred variable remuneration may be made, in whole or in part, by way of stocks and/or equity-based instruments. A deferred bonus will be granted only if, at the designated payment date, the Bank meets its capital adequacy targets. If not, the payment will be deferred until the target is met. In addition, the Bank's Board of Directors has the discretion to reduce the annual measurable bonus amount, in whole or in part, for some of, or all, of the officeholders. For key employees who are not officeholders - the President and CEO may decide, at her discretion, to reduce the amount of the variable annual bonus (in whole or in part).

e. Description of the ways in which the Bank links the remuneration to longer-term performance	
Discussion of the Bank's policy regarding the deferral and vesting of variable remuneration, and whether the deferred part of the variable bonus varies among employees or groups of employees; description of the factors determining the said part and their relative weight.	See above.
Discussion of the Bank's policy and criteria for adjusting a deferred remuneration before and after vesting by means of a claw-back arrangement	In addition to the aforesaid, a key employee must return to the Bank any amounts paid to him in accordance with the remuneration policy, if paid on the basis of data found to be erroneous and restated in the Bank's financial statements (in the manner determined by the Remuneration Committee and Board of Directors). In addition, a key employee may be required, in certain cases, to return variable remuneration paid to him. Variable remuneration is recoverable for a maximum period of 5 years from the date on which it was paid (and for officeholders - for a maximum of 7 years, in certain cases).
f. Description of the different forms of variable remuneration used by the Bank and considerations for using them	
Discussion of the ratios considered adequate between the maximum variable remuneration and the fixed remuneration set by the Bank pursuant to Section 13 to Directive 301A.	According to the remuneration policy, pursuant to Directive 301A, the maximum ratio between the fixed remuneration and the variable remuneration in a given year for each of the key employee shall not exceed 100% of the fixed remuneration of that key employee during that year. It should be noted that the variable annual bonus is limited to 6 monthly salaries; in exceptional cases, a special bonus of up to one monthly salary may be granted to a key employee.
In exceptional cases, where the Bank has determined that the maximum variable remuneration may exceed 100% of the fixed remuneration - details of the ratios set, the reasons thereto, the affected employees, their position and the effect on the Bank.	The maximum variable remuneration may not exceed 100% of the fixed remuneration.
Review of the various forms of variable remuneration (e.g., cash, shares, equity-based instruments, etc.).	As aforesaid, if the variable annual bonus for a key employee in respect of the measured year exceeds 40% of the fixed remuneration - 50% of the variable annual bonus is paid in cash and 50% over a period of three years. The deferred variable remuneration may be made, in whole or in part, by way of shares and/or equity-based instruments.
Discussion of the use of various forms of variable remuneration, and, whether the mix of the various forms of remuneration varies among employees or groups of employees, a description of the factors that determine the mix and their relative weight.	The provision in the remuneration policy whereby deferred remuneration may be paid by means of shares and/or equity-based instruments applies only to officeholders and other key employees (and does not apply to other employees of the Bank who are not key employees).

Quantitative disclosure

The number of meetings held by the entity supervising remuneration during the reporting year and the remuneration paid to its members for the reporting year.	In 2017, the Board of Directors' Remuneration Committee held 7 meetings. The total remuneration paid to the members of the Remuneration Committee for its meetings during 2017 is NIS 172,639.
The number of employees who received variable remuneration during the reporting year.	Officeholders: In 2017, a variable annual bonus was paid to 20 of the Bank's officeholders (for 2016). No. of key employees who are not officeholders: In 2017, a variable annual bonus was paid to 102 of the Bank's key employees (for 2016).
Number and total amount of guaranteed bonuses granted during the reporting year.	Officeholders: In 2017 a fixed annual bonus was granted in the total amount of NIS 0.64 million, which represents part of the fixed remuneration of said officeholders (for 2016), No. of key employees who are not officeholders: In 2017 a fixed annual bonus was granted in the total amount of approximately NIS 1 million, which represents part of the fixed remuneration of said key employees (for 2016),
Number and total amount of bonuses granted during the reporting year.	Officeholders: In 2017, 4 of the Bank's officeholders received signing bonuses totaling NIS 1.3 million. No. of key employees who are not officeholders: In 2017, one key employee received a signing bonus of NIS 0.3 million.
Number and total amount of severance pay paid during the reporting year.	Officeholders: In 2017, (supplementary) severance pay was paid to one officeholder in the total amount of NIS 0.6 million. No. of key employees who are not officeholders: In 2017, severance pay was paid to three key employees (who are not officeholders) in the total amount of NIS 4.5 million. The above does not include officeholders and other key employees who have opted to receive a defined-benefit pension and/or interim pension from the Bank under an individual employment agreement with the Bank.
The total amount of outstanding deferred remuneration, with separate disclosure for cash, shares, equity-based instruments and other forms of remuneration.	Officeholders: The total outstanding deferred annual remuneration granted to the officeholders as at December 31 2017 is 1,204,735 restricted performance share units that constitute a deferred interest, subject to the receipt of the Bank's ordinary shares at NIS 1 par value each. No. of key employees who are not officeholders: There is a deferred outstanding remuneration balance in the amount of NIS 1.62 million.

Total deferred remuneration paid during the reporting year.	Officeholders: The total outstanding deferred annual remuneration granted to the officeholders in 2017 was 523,270 restricted performance share units that constitute a deferred interest, subject to the receipt of the Bank's ordinary shares at NIS 1 par value each, and 27,138 restricted performance share units that constitute a deferred interest, subject to the receipt of the Bank's ordinary shares at NIS 1 par value each. No. of key employees who are not officeholders: In 2017, deferred remuneration in the amount of NIS 0.57 million was paid to key employees who are not officeholders.
For more information regarding the remuneration amount for the reporting year, with a distinction between remuneration that is fixed or variable, deferred or undeferred, various forms used (cash, shares, equity-based instruments and other forms), please	see the table below.
The total outstanding remuneration amount has been deferred and the retained remuneration, is subject to retroactive adjustments - explicit and/or implicit.	Officeholders: 1,204,735 restricted performance share units that constitute a deferred interest, subject to the receipt of the Bank's ordinary shares at NIS 1 par value each. No. of key employees who are not officeholders: N/A.
Total amortization amount during the reporting year due to explicit adjustments only.	N/A.
Total amortization amount during the reporting year due to implicit retroactive adjustments.	N/A.

Table 39 - Remuneration of officeholders[(a)(b)]

	For 2017		For 2016	
	Undeferred	Deferred	Undeferred	Deferred
	in NIS millions			
Fixed remuneration				
• Cash-based	**34**	**-**	30	-
• Shares and equity-based instruments	**-**	**-**	-	-
• Other	**-**	**-**	-	-
Variable remuneration				
• Cash-based	**8**	**-**	11	-
• Shares and equity-based instruments	**-**	**-**	-	9
• Other	**-**	**-**	-	-

(a) Excluding members of the Board and the Chairman of the Board (for part of 2016).
(b) In respect of signature bonuses granted in 2017; for more information, please see the quantitative section above.

Table 40 - Remuneration of other key employees

	For 2017		For 2016	
	Undeferred	Deferred	Undeferred	Deferred
	in NIS millions			
Fixed remuneration				
• Cash-based	**90**	**-**	91	-
• Shares and equity-based instruments	**-**	**-**	-	-
• Other	**-**	**-**	-	-
Variable remuneration				
• Cash-based[(a)]	**32**	**-**	34	1
• Shares and equity-based instruments	**-**	**-**	-	-
• Other	**-**	**-**	-	-

(a) The variable remuneration for 2017 is based on an estimate, since the bonus amounts have yet to be determined and paid; the variable remuneration for 2016 was revised according to actual payments.