Bank Leumi

Risk Management Report

As at December 31 2018

The Risk Management Report and description of the main characteristics of the regulatory capital instruments issued are available on the Bank's website at: www.leumi.co.il and on the Israel Securities Authority's MAGNA website, www.magna.isa.gov.il

This is a translation from the Hebrew. It has been made for convenience purposes alone. In case of any discrepancy, the Hebrew version shall prevail.

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[1] For information regarding the disclosure initials, please see the legend at the end of the report.

Part 1 - Overview

Risk Management Report

We are pleased to present the Risk Management Report as at December 31 2018 (hereinafter: the "Risk Management Report”) of Bank Leumi Le-Israel B.M. (hereinafter: the “Bank”). The Risk Management Report was prepared in accordance with the directives and guidance of the Banking Supervision Department regarding the disclosure requirements outlined in Pillar 3 of the Basel Accord and includes additional risk information.

The Report constitutes complementary, additional information to the consolidated financial statements of the Bank and the Report of the Board of Directors and Management as at December 31 2018 and should be read in conjunction with the information presented therein.

David Brodet

Chairman of the Board

Rakefet Russak-Aminoach

President and CEO

Bosmat Ben Zvi

First Executive Vice President

Head of the Risk Management Division

March 6 2019

Purpose and Disclosure Principle

The purpose of the Report is to enable users of the Bank’s reports to evaluate significant information included therein regarding the application of the Basel Committee Framework, capital, risk exposure, and risk assessment processes.

The information in the 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).

Pursuant to the Bank of Israel Circular of December 31 2017, regarding improving the usefulness of reports to the public for 2017 and 2018, the format of the risk management report of banking corporations was revised, in accordance with the provisions of the Basel Committee's Pillar 3, which were recently revised. As part of the revision, quantitative and qualitative disclosure requirements have been altered and uniform reporting tables were set to improve comparativeness in the banking sector. The 2018 Risk Management Report was prepared according to the said new format, while reclassifying the comparative data in order to adapt them to the new disclosure format. The report was also 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 provisions.
- 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 includes unaudited estimates and/or represents information which is considered forward-looking.
- Most of the qualitative information regarding risk exposures and their management is detailed in this Report. Additional relevant information may be found under Risk Review in the 2018 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 materialization 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 affect", "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 indeed materialize, 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 pursuant to any law.

Scope of Application

a. The Group is regulated by the Banking Supervision Department 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 2018, there were no differences between the scope of consolidation according to the accounting principles and the regulatory scope of consolidation for capital adequacy purposes. The data presented as part of the regulatory disclosure requirements in accordance with the Basel provisions included in this Report are based on the financial information presented in the financial statements, with the adjustments required pursuant to the implementation of the Basel provisions (such as capital deductions, debt instruments qualified for inclusion in the regulatory capital, special treatment of the accounting effect in respect of the effect of the efficiency plan on the Bank's capital and adjusted calculation in respect of special actuarial obligations).

b. The banking Group's foreign offices are regulated by the respective regulators in their countries of operation, which have adopted the Basel Committee's 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 equity and bond investments in foreign companies abroad. Any increase in investment or a decrease in holding any type of means of control to less than 80 percent requires prior approval by the Bank of Israel.
2. The US subsidiary (BLUSA) - The US authorities restrict local banks' extent of exposure - of any type - to related companies. The maximum allowed exposure rate to a related company is 10 percent of the Bank's capital in the United States, and the US subsidiary's maximum allowed exposure to the Group is 20 percent of its capital.
3. The UK subsidiary (BLUK) - The UK authorities restrict local banks' extent of exposure - of any type - to related companies. BLUK's maximum rate of exposure to the Group's companies (excluding Bank Leumi Le-Israel B.M.) is 25 percent of BLUK's capital.
   Under a waiver issued by the British regulator, BLUK may increase its exposure to Bank Leumi Le-Israel B.M. to 100 percent of the Bank's capital in England.
4. The Romanian subsidiary - The Romanian authorities restrict local banks' exposure to related companies. Bank Leumi Romania S.A.'s maximum rate of exposure to the Group's companies - including Bank Leumi Le-Israel B.M. - is 25 percent of Bank Leumi Romania's capital.

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

Part 2 – Overview of Risk Management, Key Prudential Metrics and Risk-Weighted Assets

Key Prudential Metrics (KM1)

		A	B	C	D	E
	On a consolidated basis, as at:	**December 31 2018**	September 30 2018	June 30 2018	March 31 2018	December 31 2017
	Available capital (in NIS millions)					
1	Common Equity Tier 1 capital (CET1)[(a)]	**35,190**	35,450	35,011	34,316	34,653
1A	Common Equity Tier 1 capital, before the effect of the transitional provisions and before the effect of adjustments for the efficiency plans	**34,679**	34,915	34,416	33,677	33,450
2	Tier 1 capital[(a)]	**35,190**	35,450	35,011	34,316	34,653
2A	Tier 1 capital, before the effect of the transitional provisions and before the effect of adjustments for the efficiency plans	**34,679**	34,915	34,416	33,677	33,450
3	Total capital[(a)]	**46,223**	46,277	44,781	44,074	45,464
3A	Total capital, before the effect of the transitional provisions and before the effect of adjustments for the efficiency plans	**39,894**	39,925	38,368	37,617	37,453
	Risk-weighted assets (in NIS millions)					
4	Total risk-weighted assets (RWA)[(a)]	**317,845**	314,993	313,485	308,817	303,292
	Capital adequacy ratios (in %), as per the Banking Supervision Department's directives					
5	Common Equity Tier 1 capital ratio[(a)]	**11.07%**	11.25%	11.17%	11.11%	11.43%
5A	Common Equity Tier 1 capital ratio, before the effect of the transitional provisions and before the effect of adjustments for the efficiency plans	**10.92%**	11.09%	10.98%	10.91%	11.03%
6	Tier 1 Capital ratio[(a)]	**11.07%**	11.25%	11.17%	11.11%	11.43%
6A	Tier 1 capital ratio, before the effect of the transitional provisions and before the effect of adjustments for the efficiency plans	**10.92%**	11.09%	10.98%	10.91%	11.03%
7	Total capital ratio[(a)]	**14.54%**	14.69%	14.28%	14.27%	14.99%
7A	Total capital ratio, before the effect of the transitional provisions and before the effect of adjustments for the efficiency plans	**12.56%**	12.68%	12.25%	12.19%	12.35%
11A	Minimum Common Equity Tier 1 capital ratio set by the Banking Supervision Department[(b)]	**10.25%**	10.25%	10.25%	10.25%	10.25%
12A	Common Equity Tier 1 capital ratio beyond that required by the Banking Supervision Department	**0.82%**	1.00%	0.92%	0.86%	1.18%
	Leverage ratio pursuant to the Banking Supervision Department's directives[(c)]					
13	Total exposures (in NIS millions)	**499,289**	502,536	499,799	498,316	499,026
14	Leverage ratio (in %)	**7.05%**	7.05%	7.00%	6.89%	6.94%
14A	The leverage ratio, before the effect of the transitional provisions and before the effect of adjustments for the efficiency plans (in %)	**6.95%**	6.95%	6.89%	6.76%	6.70%
	Liquidity coverage ratio pursuant to the Banking Supervision Department directives[(d)]					
15	Total high-quality liquid assets (in NIS millions)	**112,338**	117,505	117,493	118,229	113,298
16	Total cash outflows, net (in NIS millions)	**92,623**	97,405	94,613	96,909	92,757
17	Liquidity coverage ratio (in %)	**121%**	121%	124%	122%	122%

Please see comment below.

Comments:

(a) The data include adjustments for the efficiency plans prescribed in the Banking Supervision Department letter dated January 12 2016 entitled “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 July 2017, are being gradually withdrawn until June 30 2021 and June 30 2022, respectively. For more information on the effect of the transitional provisions and adjustments in respect of the efficiency plans, please see the section entitled "Relief in respect of Operational Efficiency Plans" in Part 3 below. NIS 157 million - in respect of adjustments for the efficiency plans - was added to the total balance of risk-weighted assets (NIS 127 million as at September 30 2018, NIS 179 million as at June 30 2018, NIS 192 million as at March 31 2018 and NIS 94 million as at December 31 2017).

(b) The minimum Common Equity Tier 1 capital ratio and minimum Total capital ratio are 10 percent and 13.5 percent, respectively. In addition to the above ratios, there is a capital requirement of 1 percent of the outstanding housing loans as at the reporting date. Thus, the minimum Common Equity Tier 1 capital ratio requirement and the minimum Total capital ratio requirement as at the reporting date are 10.25 percent and 13.75 percent, respectively.

(c) For more information on the leverage ratio, please see Part 4 below.

(d) The Bank's liquidity coverage ratio was calculated according to average daily observations during the reported quarter. For more information on the liquidity coverage ratio, please see Part 7 below.

Bank Risk Management Approach (OVA)

The Bank's business operations involve the management of financial and non-financial risks. The key financial risks managed by the Bank are: credit risks - which are integral to the Bank's core business, as well as market and liquidity risks. In addition to managing financial risks, the Bank's activities give rise to non-financial risks, the management of which is 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, compliance risks, reputational risks, conduct risks and strategic risk.

Leumi's risk management strategy is 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 of the Bank's business activity. The risk management framework includes risk identification and estimation mechanisms, defining organizational structure and responsibilities for their management, including adequate control and reporting mechanisms.

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

The framework used for estimating and managing risk and as a basis for 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 pursuant to the Group's strategic goals.
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 as well as assessments of the implications of scenarios of varying severity.
d. Action plans for handling and mitigating risk are drawn.

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 regulators.

Risk assessments are made at the Group-, activity- and individual transaction level, using several 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.

Information on How to Manage Risk for Each of the Key Risks can be Found Within the Report, as follows:

Disclosure topic	Overview	Credit risk[1]	Market risk, including IRRBB	Operational risk
Business model and overall risk profile	9-14	29-30	54	73
Corporate governance structure	10-14	30	54	73
Communications channels	9-14	29-30	54-55	73
Risk measurement systems	10, 13	30	56-57	73
Process of reporting risk information to the Board of Directors and management	12-13	29	54-55	73
Stress tests (qualitative information)	14		56-57	
The strategies and processes for managing, hedging and mitigating risks arising from the business model	13-14	29-30	54-57	73-75

[1] Excluding counterparty credit risk exposures and securitization exposures which are outlined in Part 5A and Appendix B, respectively.

The Business Model

Bank Leumi and its subsidiary companies constitute one of Israel's largest banking groups.
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.
In view of the new trends and significant changes introduced into its operating environment, Leumi adopted two main courses of action, the combination of which is at the core of the Group strategy. On the one hand, the Bank strives to adapt its traditional banking models without compromising the high-quality professional services it provides to all customer types according to their needs, preferences and attitude to the adoption of digital innovation; on the other hand, the Bank develops its "New Banking" model through digital and technological channels. These two courses of action depend on and are combined with the need to streamline the Bank's activity and maximize capital utilization while meeting capital adequacy targets.
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 the section entitled "Overview, Goals and Strategy" in the Annual Report of the Board of Directors and Management.

Additional Information on Risk Exposure and Assessment

Corporate Governance Structure for Risk Management at the Bank, Processes and Key Functions

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; creating a comprehensive, up-to-date picture of the risks for decision-making purposes; 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).

   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 Chief Accountant - who is responsible for financial reporting and SOX.

3. 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 audits while the challenging controls, processes and automated systems in the banking corporation. Audits are usually performed retrospectively on the first and second lines of defense, 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; approval of the organizational structure; overseeing and challenging the risk levels to which the Group and the Bank are exposed, while ensuring compliance with the risk appetite and compliance with the law and regulations.

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.

Reporting to the Chief Risk Officer are the head of a department and heads of functions managing the various risks as outlined in the diagram on the next page, as well as the Head of the Special Credit Function.

In 2018, the Risk Management Division was restructured, with the credit risk management operations merged and consolidated within the division so that the responsibility for the risk management array was extended to include enterprise-wide credit risk policy and management. In addition, a Model Risk Management Department was formed to ensure a more comprehensive view of managing model risks in the Group while adapting the tools and infrastructure required in the changing business environment. In addition, the management of the Market Risk Department and Total Return Risk Department were merged, reporting to the Risk Management Division.

The Bank is implementing a Group-wide risk management framework, which includes corporate governance and control principles, insofar as they do not contradict local law and regulatory provisions in the foreign offices. 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.

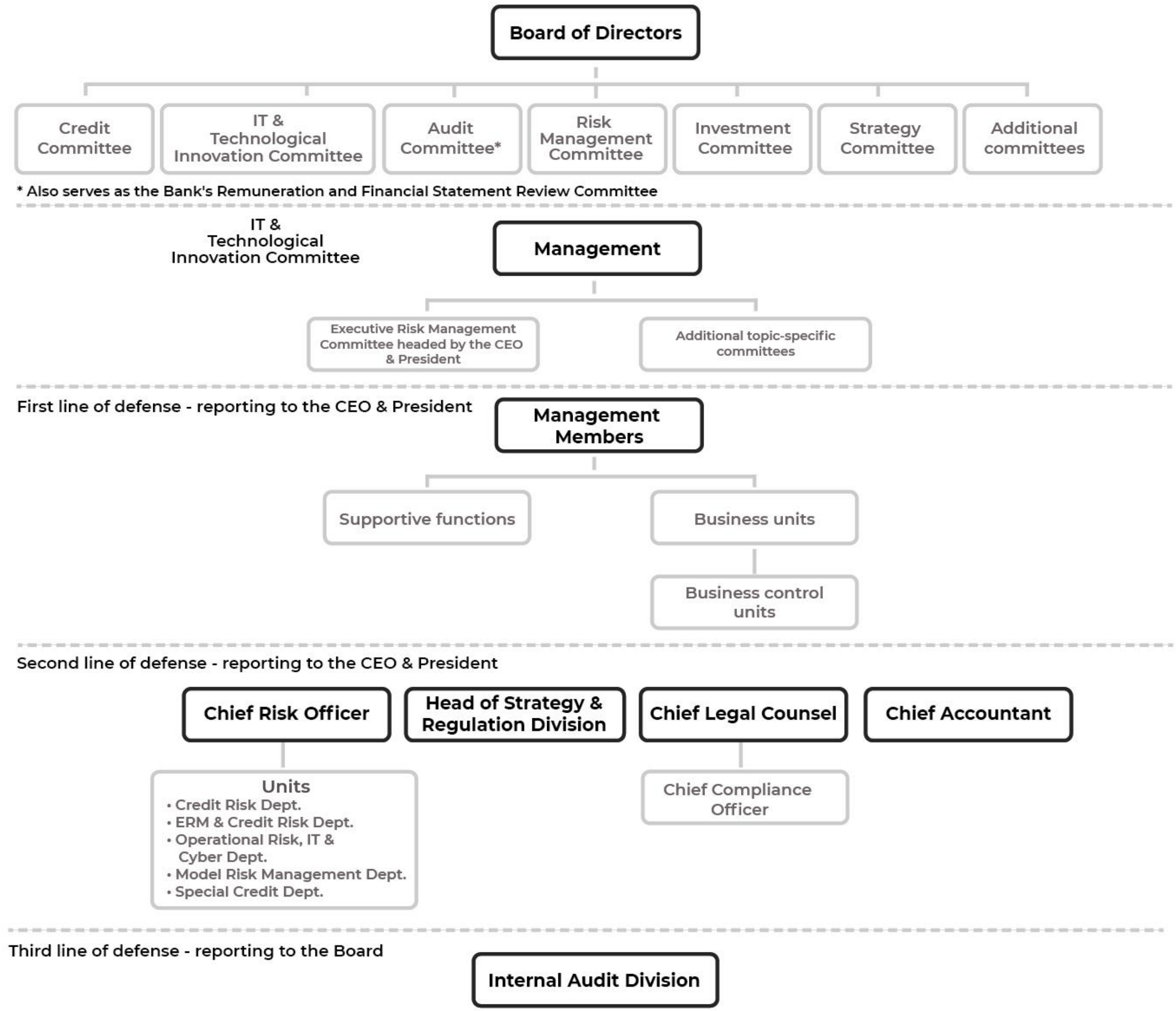
Risk management command and control is conducted by the committees responsible for managing the various risks. The various committees discuss aspects of the various risk exposures; direct the drafting of policy papers; examine the risk profile and models measuring risk exposure; and prescribe internal boundaries and control processes in accordance with the market conditions and the Bank's risk appetite. Below is a breakdown of the committees:

- The Risk Management Committee of the Board of Directors
- The Credit Committee of the Board of Directors
- 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, as follows:
    - Executive Credit Risk Management Committee
    - Executive Market Risk Management Committee.
    - Executive Operational Risk Management Committee
    - Executive Committee of Risk Management for Foreign Offices
    - 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 members of management.

Another committee of the Board of Directors is the Audit Committee.

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 areas of responsibility 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.

The Bank's Corporate Governance for Risk Management



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. 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 the 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 so as 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 taking into account the level of overlap between the risks.
- The existence of a defined organizational structure and areas of responsibility, that support and reinforce the understanding of the responsibilities and authorities of the entities responsible for risk management.
- The Bank's risk management culture encourages open communication, sharing information and conducting deliberations across the organization, which constitute another layer supporting decision-making process.
- The Bank has tools in place for risk identification and assessment, while regulating means of supervision, control and reporting.
- 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.
- The Bank promotes and assimilates a culture of fair business conduct, taking into account the customers' needs.
- The Bank's activity is managed pursuant to the principles of its Code of Ethics, which reflect the Bank's core values.

The Internal Capital Adequacy Assessment Process (ICAAP)

The Capital Adequacy Assessment Process (ICAAP) is aimed at calculating the capital required to support the various risks to which the Group is exposed - both in the ordinary course of business and under stress scenarios, in order to ensure that the Group's effective capital exceeds the capital requirements at any time. As part of the process, the risk appetite and risk bearing ability were defined, and the Group carried out a comprehensive mapping and risk assessment process of the risks to which it is exposed.

According to the process, the Bank is in possession of adequate capital and liquidity to handle all of the risks identified - both in the ordinary course of business and under extreme stress scenarios.

The products of the process are summarized in the ICAAP paper submitted to the Banking Supervision Department in January 2019.

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 forward-looking 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 reexamined each year and approved at the Board level as part of the ICAAP process. In January 2019, the Group's risk appetite was confirmed 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 metrics were set, based on forward-looking assumptions which reflect the Group's aggregate risk appetite statements.

Using Stress Testing as Part of Risk Management

Using a global stress test is an accepted global practice. It is required under the Basel Committee rules and contributes to understanding the risk exposure both at the banking system and individual bank levels. The process boosts the banking system's transparency, allows to examine the robustness of banking corporations under adverse market conditions and to draw comparisons between them. The process supports methodology improvements and the understanding of the risk factors by banking corporations as well as by the Banking Supervision Department.

Since 2012, the Bank of Israel's Banking Supervision Department has been performing a macroeconomic stress test for the banking system, based on a global scenario. In this framework, the Bank estimates - as do the other banks in Israel - the test results using a variety of models and methodologies that are also based on subjective "expert assessments".

Underlying the global stress tests for the banks are two macroeconomic scenarios devised by the Bank of Israel: A base scenario and a stress scenario, which change from year to year. It should be noted that the scenarios taken into account do not constitute forecasts, but are rather hypothetical scenarios designed to test the resilience of banking corporations under a very severe macroeconomic environment.

The Banking Supervision Department incorporates the results of the global stress test as a supplemental component of the Supervisory Review and Examination Process (SREP), including quantitative and qualitative elements. At the same time, banking corporations are required to integrate the global stress test into an internal process to assess their Internal Capital Adequacy Assessment Process (ICAAP)

During the fourth quarter of 2018, Bank Leumi performed a stress scenario based on the Bank of Israel's global stress scenario for 2018 (local stress scenario), which is spread over the years 2019-2021.

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 operating environment.

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 materialization of the various scenarios.

Risk Profile - Defining the Risk Factors' Severity

Leumi's risk profile is examined on a quarterly basis, as part of the exposure report submitted to 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 the various risks. The methodology is based on quantifying the effect of various scenarios' materialization on the Group's capital, i.e. its stability, and includes "expert assessments" by relevant functions in the Bank.

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

Most Material and Emerging Risks

In recent years, major 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. Following are the most material and emerging risks:

Strategic Risk

Strategic risk is a business risk whose damage is material and affects the business model of the Bank or of one of its business lines. In fact, this type of risk may have an effect on profit that is insignificant in the immediate term, but which may become significant in the mid- to long term.
Strategic risks involve threats that may arise from erroneous business decisions, inadequate implementation of decisions, or failure to respond to sectoral, economic, regulatory, consumer, or technological developments.

The main strategic risk stems from the fact that the financial service industry is undergoing significant digitalization changes. The opening of the banking industry to competition and the entry of new players - such as BigTech (Google, Amazon, Facebook and Apple), Fintech companies, insurers and non-banking credit companies - requires adjustment of the business model. In addition, the Law for Increasing Competition and Reducing Concentration in the Banking Market in Israel (the "Strum Law") includes components which could strategically impact the competitive map in Israel. One of its direct consequences for Bank Leumi is the sale of Leumi Card. Another strategic topic is open banking.

Strategic risk management is led by the Strategy and Regulation Department, with the involvement of the Risk Management Division and Finance Division. These functions are in charge of identifying, mapping, assessing and monitoring this risk for all of the Bank's units and the Board of Directors.

In view of the new trends and significant changes introduced into its operating environment, Leumi adopted two main courses of action, the combination of which is at the core of the Group strategy. On the one hand, the Bank strives to adapt its traditional banking models without compromising the high-quality professional services it provides to all customer types according to their needs, preferences and attitude to the adoption of digital innovation; on the other hand, the Bank develops its "New Banking" model through digital and technological channels. These two courses of action depend on and are combined with the need to streamline the Bank's activity and maximize capital utilization while meeting capital adequacy targets.

For more information, please see under "Strategic Risk" in Part 9 below.

Information Security and Cyber Risk

Leumi continues to promote the provision of financial services through digital platforms, expanding the use of advanced technologies. As a result, the risk of cyber-attacks is growing, as is Leumi's exposure to the materialization of cyber risks.

Cyberspace is highly dynamic and characterized by uncertainty in terms of the type, scope and force of the attacks. A materialization of a cyber event may result in monetary damage, theft of sensitive banking information, disruption of activity and operational continuity and even damage to the Bank's reputation.

For more information, please see under "IT and Cyber Security Risk" in Part 8 below.

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 activity. The IT environment is complex, ever-changing and organizations are becoming increasingly dependent on it.
Leumi 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.
In light of the above, and in order to ensure that the systems are up to date, that the business and technological elasticity increases and to improve the system's stability, Leumi is at the final planning stages of a project to replace its core systems. This significant project will take several years to complete, and will have milestones in line with Leumi's business lines.

Regulatory Risk

Regulatory risk is the risk of legislative and regulatory changes affecting the Group's total income and expenses, capital, areas of activity or the business environment in which it operates.

The Leumi Group operates in a complex and multidisciplinary regulatory environment. Material ongoing changes in diverse regulatory domains require adequate ongoing preparedness of the Bank's activities.

Recently, significant emphasis has been made on provisions designed to encourage new players to enter into traditional banking, removing barriers and restrictions, as well as provisions intended to promote innovation in the financial system, such as: The provisions of the Law for Increasing Competition and Reducing Concentration in the Banking Market in Israel, a new policy for establishing a banking corporation by the Bank of Israel, promoting the adoption and implementation of the Open API standard designed to enable sharing of financial information between customers and third parties, and new advanced payment legislation.

In addition, the consumer regulation trend continues, including legislation aiming to reduce costs for customers. At the same time, emphasis is made on adapting the various financing products to customers' needs, while providing maximum disclosure and stressing transparent and fair conduct.

Additional trends are manifested in handling the transition to e-banking, outsourcing and use of cloud computing in the financial system, as well as privacy protection and cyber defense. These topics are on the agenda both in Israel and globally, and are reflected in the GDPR requirements, which deal with privacy protection as well as specific cybersecurity and outsourcing directives

The abovementioned changes affect and are expected to continue affecting the banking industry in the coming years. The Bank monitors and identifies relevant regulatory provisions and examines its preparedness to the following: Changing market conditions; increased competition and transparency; entry of new players into traditional banking domains; the Bank's costs compared to those of other entities; use of databases and information of the Bank's customers by non-banking entities as well as providing adequate value propositions to the Bank's customers. At the same time, regulation erodes income, leads to increased compliance costs and requires banks to constantly improve their levels of service and innovation.

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 foresee that outcome. As a result, the Bank may incur losses from lawsuits, 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.

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. Lately, some risks have risen from possible international trade developments, especially the trade relations between the US and China. If the situation escalates to an ongoing "trade war", it may have an adverse effect on global growth. As a result, the Israeli economy may be indirectly affected as well.

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.

Overview of Risk-Weighted Assets (OV1)

		A	B	C
		December 31 2018	September 30 2018	**December 31 2018**
		Risk-weighted assets		Minimum capital requirements[a]
		In NIS millions		
1	Credit risk (standardized approach) [b]	**270,036**	269,084	**37,130**
6	Counterparty credit risk (standardized approach)	**4,358**	4,534	**599**
10	Credit valuation adjustment (CVA)	**1,518**	1,795	**209**
16	Securitization exposures (standardized approach)	**411**	419	**57**
25	Amounts below the thresholds for deduction (subject to 250% risk weight)	**12,514**	12,617	**1,721**
	Total credit risk	**288,837**	288,449	**39,716**
20	Market risk (standardized approach)	**6,295**	4,059	**866**
24	Operational risk	**22,713**	22,485	**3,123**
27	Total	**317,845**	314,993	**43,705**

(a) Capital requirements in accordance with the minimum total capital ratio, at a rate of 1 percent of the outstanding housing loans as at the reporting date, for a total of 13.75 percent.

(b) Credit risk does not include counterparty credit risk, credit valuation adjustment, settlement risk, securitization exposures and amounts below the deduction thresholds.

Additional Information on Risk-Weighted Assets

Movements in Risk-Weighted Assets

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

Movement in Credit Risk-Weighted Assets[(a)]

	For the year ended December 31	
	2018	2017
	In NIS millions	
Opening balance	**277,344**	266,534
Change in transactions	**7,898**	12,117
Collateral insurance pursuant to the Sales Law	**598**	81
Rating changes	**(154)**	(315)
Exchange rate differentials	**2,887**	(2,433)
Entry into/exit from credit default	**634**	494
Net derivative transactions	**1,042**	951
Change in CVA	**(156)**	267
Offset of payroll tax by deferred taxes	**690**	771
Effect of change of the conversion rate coefficient of Sale Law guarantees to 30%	**(3,210)**	-
Other	**1,264**	(1,123)
Closing balance	**288,837**	277,344

(a) Movement includes amounts related to credit risk, counterparty credit risk, securitization exposures and amounts below the thresholds for deduction, subject to a 250 percent risk weight.

Movement in Market Risk-Weighted Assets

	For the year ended December 31	
	2018	2017
	In NIS millions	
Opening balance	**4,464**	4,788
Interest rate risk - change in open positions	**19**	(264)
Foreign currency risk - change in open positions - USD, GBP, euro and yen	**358**	128
Equity risk - change in futures and options on stock indices	**(130)**	(197)
Options risk - change in currency options - NIS/forex and forex/forex	**1,584**	9
Closing balance	**6,295**	4,464

Changes in Operational Risk-Weighted Assets

	For the year ended December 31	
	2018	2017
	In NIS millions	
Opening balance	**21,484**	20,843
Change	**1,229**	641
Closing balance	**22,713**	21,484

Components of Risk-Weighted Assets by Business Activity

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 2018										
	Activity in Israel									Foreign operations	Total
	Households	Private banking	Small- and micro-businesses	Mid-sized businesses	Corporations	Institutionals	Financial manage-ment	Other segment	Total for Israel		
	In NIS millions										
Credit Risk	**69,556**	**312**	**50,071**	**27,472**	**75,728**	**647**	**15,938**	**17,897**	**257,621**	**31,216**	**288,837**
Market risk	**-**	**-**	**-**	**-**	**-**	**-**	**6,259**	**-**	**6,259**	**36**	**6,295**
Operational risk	**7,133**	**456**	**4,569**	**1,746**	**3,254**	**475**	**1,802**	**373**	**19,808**	**2,905**	**22,713**
Total risk-weighted assets	**76,689**	**768**	**54,640**	**29,218**	**78,982**	**1,122**	**23,999**	**18,270**	**283,688**	**34,157**	**317,845**

	December 31 2017										
	Activity in Israel									Foreign operations	Total
	Households	Private banking	Small- and micro-businesses	Mid-sized businesses	Corporations	Institutionals	Financial manage-ment	Other segment	Total for Israel		
	In NIS millions										
Credit Risk	68,519	378	49,898	25,770	72,752	261	15,932	15,251	248,761	28,583	277,344
Market risk	-	-	-	-	-	-	4,416	-	4,416	48	4,464
Operational risk	6,974	450	3,627	1,803	3,114	392	2,255	422	19,037	2,447	21,484
Total risk-weighted assets	75,493	828	53,525	27,573	75,866	653	22,603	15,673	272,214	31,078	303,292

Capital and Leverage

Part 3 - Composition of Capital

Composition of the Bank's Regulatory Capital (CC1)

		December 31 2018		December 31 2017		
		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				
	Common Equity Tier 1 Capital: Instruments and Reserves					
1	Common share capital issued by the banking corporation and premium on ordinary shares included in CET1 capital	**8,168**	-	8,839	-	1
2	Reserves, including dividend proposed or declared after the balance sheet date	**29,211**	-	27,341	-	2
3	Accumulated other comprehensive income and reserves for which disclosure was made	**(2,074)**	-	(2,423)	(590)	3
5	Common share capital issued by subsidiaries of the banking corporation which were consolidated and held by a third party (minority interests)	**399**	-	229	39	4
6	Common Equity Tier 1 capital before regulatory adjustments and deductions	**35,704**	-	33,986	(551)	-
	Common Equity Tier 1 Capital: regulatory adjustments and deductions					
8	Goodwill	**178**	-	203	-	6
10	Deferred tax assets that rely on future profitability of the banking corporation	**2**	-	2	-	8
14	Unrealized profits and losses resulting from changes in the fair value of liabilities arising from changes in the banking corporation's own credit risk	**17**	-	35	9	9
21	Deferred taxes receivable incurred as a result of timing differences; whose total exceeds 10%of the CET1 capital	**1,306**	**(53)**	1,681	420	10
26	Additional regulatory adjustments and deductions established by the Banking Supervision Department	**(989)**	-	(2,588)	(312)	-
26C	Of which: Calculation of the regulatory capital, based on an eight-quarter average capitalization rate of the pension obligation	**822**	-	(749)	-	-
26D	Of which: For the effect of the efficiency plans	**(509)**	-	(592)	-	-
26E	Of which: Deduction of salary tax component from deferred tax asset	**(1,302)**	-	(1,247)	(312)	-
28	Total regulatory adjustments and deductions to Common Equity Tier 1 capital	**514**	-	(667)	-	
29	Common Equity Tier 1 capital	**35,190**	-	34,653	-	
45	**Tier 1 capital**	**35,190**	-	34,653	-	
	Tier 2 capital: Instruments and provisions					
46	Instruments issued by the banking corporation (that are not included in Common Equity Tier 1 capital) and premium on these instruments	**1,751**	-	926	-	11A
47	Tier 2 capital instruments issued by the corporation that qualify for inclusion in regulatory capital in transitional period	**5,818**	-	6,816	-	11
48	Tier 2 capital instruments issued by subsidiaries of the banking corporation and to third party investors	**220**	-	31	-	5
49	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	**220**	-	31	-	-
50	Collective provisions for loan losses before relevant tax effect	**3,243**	-	3,038	-	12
51	Tier 2 capital before deductions	**11,033**	-	10,811	-	
58	**Tier 2 capital**	**11,033**	-	10,811	-	
59	**Total capital**	**46,223**	-	45,464	-	

		December 31 2018		December 31 2017		
		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				
	Total risk assets weighted in accordance with the treatment required before adoption of Directive No. 202 pursuant to Basel III	**(53)**	-	322	-	-
	Of which: Other deferred tax assets	**(53)**	-	322	-	13
60	Total risk-weighted assets	**317,845**	-	303,292	-	-
	Capital ratios and buffers (in %)					
61	Common Equity Tier 1 capital (as a percentage of risk-weighted assets)	**11.07%**	-	11.43%	-	-
62	Tier 1 capital (as a percentage of risk-weighted assets)	**11.07%**	-	11.43%	-	-
63	Total capital (as a percentage of risk-weighted assets)	**14.54%**	-	14.99%	-	-
	Minimum requirements set by the Banking Supervision Department					
69	Minimum CET 1 capital set by the Banking Supervision Department	**10.25%**	-	10.25%	-	-
71	Minimum total capital ratio set by the Banking Supervision Department	**13.75%**	-	13.75%	-	-
	Amounts below the deduction threshold (before risk weighting)					
72	Investments in equity of financial corporations (excluding banking corporations and their subsidiaries) not exceeding 10 percent of the common share capital issued by the financial corporation and which are below the deduction threshold	**422**	-	310	-	14
73	Investments in Common Equity Tier 1 capital (excluding banking corporations and their subsidiaries) exceeding 10 percent of the common share capital issued by the financial corporation and which are below the deduction threshold	**97**	-	251	-	15
75	Deferred taxes receivable incurred as a result of timing differences that are below the deduction threshold	**3,530**	-	3,471	-	16
	Ceiling for including provisions in Tier 2					
76	Provision that qualifies for inclusion in Tier 2 relating to exposures under the standardized approach, prior to implementing the ceiling	**3,243**	-	3,038	-	-
77	Ceiling for inclusion in Tier 2 under the standardized approach	**3,610**	-	3,467	-	-
	Capital instruments not qualified as regulatory capital subject to the transitional provisions					
84	Amount of the present ceiling for instruments included in Tier 2 capital subject to the transitional provisions	**5,818**	-	7,272	-	-
85	Amount deducted from Tier 2 capital due to the ceiling	**755**	-	-	-	-

Reconciliation of regulatory capital components to balance sheet

For the disclosure of the regulatory capital components to balance sheet, please see Addendum A to the Report.

Information on Capital and Capital Adequacy

Equity attributable to the Bank's shareholders totaled NIS 35,305 million as at December 31 2018 compared with NIS 33,167 million as at the end of 2017, a 6.4 percent increase. The increase stems mainly from the net income for the period and from other comprehensive income on the back of a decrease in the negative adjustments in respect of an increase the discount rate, which was partially offset by a decrease in capital reserve om respect of available-for-sale securities. The increase was partially offset by a dividend distribution made during the period and the Bank's share buyback plan.

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 Banking Supervision Department's Proper Conduct of Banking Business Directive No. 202.

The capital to balance sheet ratio reached 7.7 percent as at December 31 2018, compared with 7.4 percent as at December 31 2017.

Regulatory Capital Structure

In May 2013, the Banking Supervision Department published the final directives for the implementation of Basel III in Israel, by amending Proper Conduct of Banking Business Directives Nos. 201-211 (hereinafter in this section - the "Directives"). The Directives went into effect on January 1 2014, subject to the transitional provisions included in the Banking Supervision Department's 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."

Common Equity Tier 1 Capital and Additional Tier 1 Capital

Common Equity Tier 1 Capital includes the banking corporation' shareholders' equity, 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.

Additional adjustments to Common Equity Tier 1 capital arising from the implementation of operational efficiency plans and the method of calculating the capitalization 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.

Tier 2 Capital

Tier 2 capital mainly includes capital instruments and the balance of the Group's loan loss provisions, subject to the ceiling prescribed by the directives.

As at December 31 2013, capital instruments included in Tier 2 capital are subject to transitional provisions and a recognition ceiling, as prescribed by the Directives, such that the amount recognized in effect 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 percent until January 1 2022. The recognition ceiling for 2018 was 40 percent.

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 are as follows: (1) A mechanism for absorbing reserve losses by way of conversion to common shares or amortization of the instrument when the banking corporation's Common Equity Tier 1 capital ratio falls below 5 percent; (2) A clause determining that, on the occurrence of the trigger 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 common shares or written off.

For information regarding subordinated bonds issued by the Bank in 2018 and which are qualified for inclusion in Tier 2 Capital, please see the section entitled “Bonds, Capital Notes and Subordinated Bonds” in the Report of the Board of Directors and Management.

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.

Movement in the Composition of the Regulatory Capital

	For the year ended December 31	
	2018	2017
	In NIS millions	
Common Equity Tier 1 capital		
Balance at beginning of period	**34,653**	32,586
Non-cash issue	**(29)**	1
Increase (decrease) in premium	**(642)**	7
Net income for the period less dividend	**1,870**	2,549
Retained earnings reserves in respect of associates	**10**	12
Unrealized gains (losses) from adjustments of available for sale securities	**(393)**	168
Capital reserve for stock-based payment transactions	**(8)**	-
Capital reserves in respect of employee benefits	**605**	(1,059)
Increase in capital reserves (other and associates)	**28**	2
Effect of the efficiency plans	**(61)**	124
Effect of transitioning to the pension obligation capitalization rate according to an 8-quarter moving average	**(1,108)**	395
Movement in the translation differences reserve in respect of subsidiaries	**107**	(131)
Minority interests	**170**	(16)
Regulatory adjustments and deductions		
Goodwill and intangible assets	**25**	59
Deferred taxes in respect of future profitability	**-**	(1)
Change in deferred taxes as a result of capitalization of pension obligation according to moving average	**(464)**	153
Change in deferred taxes as a result of the efficiency plans	**(21)**	71
Deferred taxes in respect of timing differences	**430**	(251)
Accumulated gains/losses arising from changes in own credit risk for financial liabilities at fair value	**18**	(16)
Net increase in Common Equity Tier 1 capital	**537**	2,067
Balance as at end of period	**35,191**	34,653
Tier 2 capital		
Balance at beginning of year	**10,811**	11,850
Deduction of subordinated bonds pursuant to the transitional provisions	**(999)**	(899)
Issuing qualifying subordinated bonds	**825**	-
Minority interests	**190**	10
Movement in general provision	**206**	(150)
Net increase (decrease) in Tier 2 capital	**222**	(1,039)
Balance as at end of period	**11,033**	10,811
Total capital as at the end of period	**46,224**	45,464

See note below.

Note:
In 2018, the changes in the regulatory capital arise mainly from a net income for the period less dividends in the amount of NIS 1,870 million; a decrease in negative capital reserves for employee benefits in the amount of NIS 605 million due to the ending of the transitional provisions period for deductions from capital, including the employee benefits reserve; a decrease in the effect of transitioning to an average curve in the amount of NIS 1,108 million; unrealized losses from reconciliation of available-for-sale securities in the amount of NIS 393 million; an increase in capital as the result of changes in deferred taxes attributed to timing differences in the amount of NIS 430 million; a decrease in regulatory capital instruments in the amount of NIS 999 million, due to the effect of the decrease in the recognition ceiling from 50 percent to 40 percent for these instruments, which no longer qualify and are subject to deduction pursuant to the transitional provisions; and an increase in the Tear 2 Capital due to the issue of qualified bonds totaling NIS 825 million.

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 percent to 50 percent for these instruments, which no long qualify and are subject to deduction pursuant to the transitional provisions.

The Banking Corporation's Approach to Assessing Capital Adequacy

The Bank implements the capital measurement and adequacy directives according to the Basel III rules, as adopted by the Banking Supervision Department 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 applies the standardized approach to 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 book's interest risk and pension risk. At the same time, the Banking Supervision Department 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 percent 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 percent and a total capital ratio of at least 13.5 percent, 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 percent of the outstanding balance of its housing loans. The effect of this requirement on the capital ratio in the reporting period is 0.25 percent.
As a result, the minimum capital requirements applicable to the Bank as of December 31 2018 are 10.25 percent for the Common Equity Tier 1 capital ratio and 13.75 percent 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 has set capital targets in case of a stress scenario event.

Under the regulatory review process, the Banking Supervision Department 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 percent, 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 a 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 discount 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 beginning 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 the section entitled "Critical Accounting Policies and Estimates, Controls and Procedures" 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 entitled "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, whereby it will be able to spread the effect of the plan on the capital ratios and leverage ratio 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 2018, 50 percent of the plan's costs are attributable to regulatory capital.

In June 2017, the Banking Supervision Department published an additional circular entitled "Increasing Operational Efficiency of the Banking System in Israel - Increasing Efficiency in Real Estate." The circular extended the relief in respect of increasing manpower efficiency until 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). As of December 31 2018, 30 percent of the plan's costs are attributable to regulatory capital.

In September 2018, the Banking Supervision Department published a letter regarding the extension of the validity of the two letters by 18 additional months, until December 31 2019, in an effort to allow for additional efficiency plans.

Regulatory and Other Changes in Measuring the Capital Requirements

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 in 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 global standardized approach was prescribed with regard to operational risk, and changes were made in market risk measurement. 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.

Revision of Proper Conduct of Banking Business Directive No. 203, "Measurement and Capital Adequacy - The Standardized Approach - Credit Risk"

On March 15 2018, the Bank of Israel published an amendment to Proper Banking Management Directive No. 203, pursuant to which mortgages with an LTV ratio of 60 to 75 percent will be risk-weighted by 60 percent only, instead of 75 percent.

Revision of Proper Conduct of Banking Business Directive No. 203, "Measurement and Capital Adequacy - Credit Risk - The Standardized Approach" and Proper Conduct of Banking Business No. 313, "Limitations on Indebtedness of a Borrower and a Group of Borrowers"

On November 13 2018, the Bank of Israel published a circular revising Proper Conduct of Banking Business Directives Nos. 203 and 313. According to the draft, the conversion coefficient for loans on collateral for guaranteeing investments of apartment buyers granted pursuant to the Sale Law (Apartments), 1974, shall be 30 percent in lieu of 50 percent if the apartment has yet to be delivered to the buyer. The effect of the circular's implementation is a 0.1 percent improvement in the Common Equity Tier 1 capital ratio.

Circulars on Amendment of Proper Conduct of Banking Business Directives following the Law for Increasing Competition and Reducing Concentration in the Banking Market in Israel (the "Strum Law")

In July 2018, the Bank of Israel published circulars on amendment of Proper Conduct of Banking Business Directives, with the objective of granting the credit companies relief immediately following their split from the banks. Inter alia, according to one of the amendments, the banks would weight credit granted to credit card companies similarly to credit granted to banks, even after their split from the banking corporation under the Strum Law. I.e., the credit card company's risk weight will be inferior by one rank from the weight of the risk weight derived from the State of Israel's rating. In addition, a debt whose original term to maturity is up to three months will be weighted at a risk weight of 20 percent.

Circular Entitled "Revision of Proper Conduct of Banking Business Directive No. 332, Buybacks by Banking Corporations"

On February 28 2019, the Bank of Israel published a circular entitled "Revision of Proper Conduct of Banking Business Directive No. 332, Buybacks by Banking Corporations." The revision revokes the prohibition on performing buybacks and allows banking corporations to purchase their own stock subject to certain terms and conditions. The revision also amends the restrictions imposed on granting loans guaranteed by securities issued by the banking corporation.

Sale of 15 Percent of BLC

On May 22 2018, the transaction for incorporating strategic partners into BLUSA was completed. Under the terms and conditions of the agreement, each of the partners acquired 7.5 percent of the equity capital of Bank Leumi Corporation, an American corporation through which the Bank holds a controlling interest in BLUSA. Under the terms and conditions of the agreement, the consideration paid for the sold equity was NIS 141 million. The transaction was accounted for as a capital transaction, with the difference between the consideration and the non-controlling interest stated directly in capital.

For more information regarding investee companies, please see the section entitled "Major Investees" in the Report of the Board of Directors and Management and Note 36 to the Financial Statements.

Sale of Leumi Card Ltd.

Pursuant to the provisions of the Law for Increasing Competition and Reducing Concentration in the Banking Market in Israel (Legislative Amendments), 2017, the Bank sold its interests in Leumi Card Ltd.

For more information regarding the said sale agreement, please see the section entitled "Major Investees" - "Leumi Card" in the Report of the Board of Directors and Management.

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 318 billion at the end of December 2018. Every 1 percent increase in risk-weighted assets (about NIS 3.2 billion) will reduce the Common Equity Tier 1 capital ratio by 0.11 percent, and the total capital ratio by 0.14 percent.
- Accrued profit or a change in the capital reserve – Leumi's Common Equity Tier 1 capital totaled NIS 35.2 billion as at December 31 2018. Total capital amounted to NIS 46.2 billion. Accrual of net income and/or positive change in

the capital reserve of every NIS 1 billion will improve the Common Equity Tier 1 capital ratio and the total capital ratio by 0.31 percent.

- 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 bond curve and by the U.S. AA corporate bond spread. A change of 0.1 percent across the discount rate curve, under the assumption that the curve rises and falls uniformly, signifies a cumulative effect of 0.06 percent on the Common Equity Tier 1 capital ratio and total capital ratio. Of which, according to a moving average calculation for eight quarters, effect of 0.01 percent on 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 November 20 2017, the Bank's Board of Directors approved a dividend distribution policy, under which the Bank will distribute, each quarter, a dividend of up to 40 percent 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 after the dividend distribution as well.

On March 6 2019, the Bank's Board of Directors approved a change in its dividend distribution policy, under which the Bank will distribute, each quarter, a dividend of up to 50 percent 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 to the provisions of the law which apply to dividend distribution, including the provisions of the Companies Law and the directives of the Bank of Israel.

On March 6 2019, the Board of Directors approved, in respect of Q4 2018, a dividend of 40 percent of the net income of the quarter. The dividend approved amounted to NIS 275 million, which is 18.401 agorot per share of NIS 1 par value. The final dividend per share amount is subject to changes due to the Bank's share issue following the vesting of PSUs, subject to meeting the terms and conditions for the vesting of the PSUs. If the said PSUs vest as aforesaid, the dividend amount for each NIS 1 share shall be 18.395 agorot. The Board of Directors has set March 26 2019 as the record date for dividend payment and April 3 2019 as the payment date.

For more information regarding the vesting of the PSUs, please see Note 25A to the financial statements.

Details on Paid Dividend

Declaration date	Payment date	Dividend per share	Cash dividend
		In agorot	In NIS millions
May 25 2017	June 22 2017	8.17	124
August 15 2017	September 11 2017	11.50	175
November 21 2017	December 21 2017	21.51	328
March 6 2018	March 28 2018	22.41	342
May 24 2018	June 19 2018	19.18	292
August 14 2018	September 6 2018	23.96	361
November 12 2018	December 10 2018	25.08 [1]	375

The Bank's Share Buyback Plan

During 2018, the Bank carried out a buyback plan of approximately NIS 700 million according to a safe harbor protection mechanism published by the Israel Securities Authority (Legal Position No. 8-199). The buyback was carried out in two stages. The first stage, pursuant to the said plan, started on May 27 2018 and ended on August 2 2018; as part of this stage, an external Stock Exchange member purchased 13,667,294 shares for approximately NIS 303 million. The second stage started on August 15 2018; as part of this stage a total of approximately NIS 397 million were transferred to another external Stock Exchange member for the purpose of continuing the buyback in accordance with the plan. The buyback plan, in which an external Tel Aviv Stock Exchange member purchased 30,412,578 shares for approximately NIS 700 million, was completed on November 22 2018.

[1] Further to the supplementary report dated November 25 2018.

Part 4 - Leverage Ratio

Expressed as a percentage, the leverage ratio is defined as the measured regulatory capital divided by the measured exposure. The regulatory capital for the purpose of leverage ratio measurement is Tier 1 capital, as defined in Proper Conduct of Banking Business Directive No. 202, taking into account the transitional arrangements. A banking corporation's measured exposure is the sum of the balance sheet exposures, exposures to derivatives, exposures to securities financing transactions and off-balance sheet items. The leverage ratio metric 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, inter alia: The effect of the implementation of the efficiency plan and adjustments in respect of the application 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.

Comparison of Accounting Assets vs. Leverage Ratio Exposure Measure (LR1)

		December 31	
		2018	2017
		In NIS millions	
1	Total assets according to the consolidated financial statements	**460,657**	450,838
	Adjustments for:		
4	Derivative financial instruments	**(3,649)**	186
6	Off-balance sheet items	**39,690**	45,524
7	Other	**2,591**	2,478
8	Exposure for leverage ratio purposes	**499,289**	499,026

Leverage ratio (LR2)

		December 31	
		2018	2017
	Item	In NIS millions	
	Balance sheet exposures		
1	Balance sheet assets (excluding derivatives and securities financing transactions but including collateral)	**446,836**	440,454
2	Amounts for assets deducted for the purpose of determining Tier 1 capital	**(314)**	(302)
3	**Total balance sheet exposures** (excluding derivatives and transactions to finance securities)	**446,522**	440,152
	Exposures for derivatives		
4	The replacement cost associated with all derivative transactions	**1,842**	1,401
5	Additional amounts in respect of potential future exposure associated with all derivative transactions	**11,181**	10,274
7	Deductions of debtors' assets in respect of variable cash collateral provided in derivative transactions	**(3,921)**	(1,916)
11	**Total exposures for derivatives**	**9,101**	9,759
	Exposures for securities financing transactions		
12	Gross assets for securities financing transactions (excluding recognition of offsets), after adjustments for transactions accounted for as an accounting sale	**1,366**	1,376
15	Exposures for securities financing transactions as agent	**2,610**	2,215
16	**Total exposures for securities financing transactions**	**3,976**	3,591
	Other off-balance-sheet exposures		
17	Total off-balance-sheet exposure at a gross nominal value	**128,327**	125,966
18	Adjustments for conversion to credit-equivalent amounts	**(88,637)**	(80,442)
19	**Off-balance sheet items**	**39,690**	45,524
	Capital and total exposures		
20	**Tier 1 capital**[(a)]	**35,190**	34,653
21	**Total exposures**[(a)]	**499,289**	499,026
	Leverage ratio		
22	**Leverage ratio in accordance with Proper Conduct of Banking Business Directive No. 218**	**7.05%**	6.94%

(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 0.01 percent as at December 31 2018 (0.09 percent as at December 31 2017). For more information on the effect of the transitional provisions and adjustments in respect of the efficiency plans, please see the section entitled "Relief in respect of Operational Efficiency Plans" in Part 3 of the Report.

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.

Credit Risk

Part 5 - Credit Risk

General Qualitative Information about Credit Risk (CRA)

Credit granting is a core activity of the Bank and the Group, which is conducted in a decentralized manner by several 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, such as: loans to the public, loans to banks, loans to governments, deposits with banks, investments in bonds.

The Bank applies a comprehensive risk management policy in line with the requirements of Proper Conduct of Banking Business Directive No. 311, "Credit Risk Management" and Proper Conduct of Banking Business Directive No. 314, "Sound Credit risk Assessment and Valuation for Loans", including the responsibility 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 by implementing corporate governance which includes three "lines of defense".

The Bank's credit policy paper reflects its respective risk appetite and is in line with the strategy.

A review of the exposure to credit risks and a snapshot of meeting restrictions is presented to Management and the Board of Directors at least once every quarter.

The Bank's credit policy is a key component of the Bank's credit management and is based on the Leumi Group's risk appetite in the credit domain. The Bank's credit policy is derived from the Group's credit policy, which serves as a master document outlining the governing principles for the Bank's policy framework both in Israel and for its foreign operations. The paper also includes a set of credit restrictions, which are defined and managed at the group level, alongside the existing procedures for identifying, measuring, monitoring, supervision and control over the credit risk. Credit policy and existing procedures which relate to the credit risk inherent in all of the Bank's activities and applies to each loan as well as to the entire loan portfolio.

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

- Maintaining proper conduct: Ethics, fairness, fair disclosure and transparency, including compliance with regulatory provisions.
- Focusing the exposures on activities for which the Bank has the expertise needed to estimate and manage the risks embodied therein.
- Dividing customer care between various business lines according to various criteria.
- Separating between the function assuming the risk and the independent function performing control over the risk and managing the risk.
- 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, including in terms of compliance.
- Ongoing and periodic monitoring of credit exposures in order to identify weaknesses as early as possible and prepare accordingly.
- Quantitative assessment of credit risk, while assigning each customer an internal risk rating.
- Setting internal quantitative boundaries and monitoring conformance thereto.
- Developing an outline which distinguishes between types of activities and economic sectors, including categories defined by various risk levels.
- Underwriting considerations include, among other things:

- Characteristics a borrower is required to have for credit approval purposes: evaluation of repayment capacity; internal credit rating; business experience; financial data and various prerequisites for credit provision (e.g., LTV ratio, maximum exposure and acceptable collateral).
- The credit authority hierarchy defines who is authorized to approve exceptional credit applications, including the pricing component.

It should be noted that there were no material changes in the Bank's credit policy in 2018.

The Subsidiaries’ Credit Policies

Each of the Bank's subsidiaries - including its foreign offices - engaged in credit granting has a credit policy paper based on the principles set forth in the Group policy paper and approved by the subsidiary’s Board of Directors. The subsidiaries’ policy papers and their conformance to the Group’s policy are also reviewed by the Risk Management Division in Israel.

As with the parent company, the credit policy of the foreign offices is based on the credit policy of guiding principles for underwriting and credit management at the individual customer level as well as on setting boundaries and managing the segments at the aggregate level.

The Corporate Governance Structure and Responsibility for Credit Risk Management

In addition to the corporate governance structure of risk management at the Bank, which is described in the above section entitled "Additional Information on Risk Exposure and Assessment", following is additional information regarding credit risk management:

First Line of Defense - The Business Lines

First line of defense includes the business units operating in the various business lines and dedicated units handling borrowers in difficulty ("troubled debt centers” reporting to the Banking Division). Please see also information about the Special Credit Department below.

Second Line of Defense - The Risk Management Division, the Accounting Division and the Legal Counsel Department - The Compliance Array

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

1. The credit risk functions - In 2018, the Risk Management Division was restructured, with the credit risk management functions merged and consolidated within the Division so that the responsibility for the risk management functions was extended to include - beyond the assessment of each individual transaction - the handling of enterprise-wide credit risk policy and management (development of the credit policy, setting boundaries and risk appetite, analysis of the credit portfolio risk at the Group level, and supervision over control of credit risk management in the foreign offices).
2. The Model Risk Department is responsible for the validation of internal models for credit risk at the Bank and its subsidiaries.
3. The Special Credit Department - The Department handles, directly and indirectly (through consulting) struggling corporate customers. The department attempts to facilitate the recovery of active customers by providing business assistance and support or by taking steps to collect the debts owed to corporate customers the recovery of whose business is impossible.

The Accounting Division - serves as the professional anchor for understanding and analyzing novel issues and relevant new regulation. In this context, in complex cases, the Accounting Department serves as a professional source of knowledge for reaching decisions about provisions and classifications.

The Legal Counsel Department, Compliance Department - Serves as a professional anchor for setting the rules for identification, documentation and assessment of the compliance risks embodied in the business activity, including aspects of prohibition of money laundering and terrorist financing, conflicts of interest and the Bank's conduct towards its customers.

Third Line of Defense - the Internal Audit Division

The Internal Audit Division is responsible for conducting independent, objective audits while challenging the controls, processes and automated systems in the banking corporation. Audits are usually performed retrospectively on the first and second lines of defense, ensuring implementation of the instructions of management and the Board of Directors

Credit Risk Management Tools - Risk Measurement Systems

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 the portfolio's quality over time.

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

- A rating system for retail customers (including housing loans), which is based on the characteristics of the customer's activity in the account over time.
- A rating system designed for business-commercial borrowers, which is based on structured expert questionnaires.

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

Credit Quality of Assets (CR1)

		A	B	C	D
		December 31 2018			
		Gross balances[a]			
		Impaired or in arrears of 90 days or more	Other	Provisions for loan losses or impairments	Net balances (A+B+C)
		In NIS millions			
1	Debts, excluding bonds	**3,850**	**294,649**	**(3,523)**	**294,976**
2	Bonds	**8**	**53,234**	**(19)**	**53,223**
3	Off-balance sheet exposures	**226**	**127,442**	**(477)**	**127,191**
4	Total	**4,084**	**475,325**	**(4,019)**	**475,390**

		A	B	C	D
		December 31 2017			
		Gross balances[a]			
		Defaulted or in arrears of 90 days or more	Other	Provisions for loan losses or impairments	Net balances (A+B+C)
		In NIS millions			
1	Debts, excluding bonds	4,341	279,403	(3,216)	280,528
2	Bonds	7	59,983	(3)	59,987
3	Off-balance sheet exposures	253	125,094	(484)	124,863
4	Total	4,601	464,480	(3,703)	465,378

(a) In accordance with the accounting values reported in the financial statements of balance-sheet items and off-balance-sheet items creating credit risk exposure in accordance with Proper Conduct of Banking Business No. 203.

Changes in Stock of Defaulted Loans and Debt Securities (CR2)

For more information regarding balance and movement in impaired debts, please see the section entitled “Credit Risks" in the Report of the Board of Directors and Management and in Note 30 to the Financial Statements.

Additional Disclosure Related to the Credit Quality of Assets (CRB)

The Bank implements the Reporting to the Public Directives on impaired debts, credit risk, and provision for loan 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 loan loss provision.

Impaired Debt

Debt is classified as impaired when the Bank is unlikely to collect all the amounts it is due under the contractual terms of the debt agreement, based on information and current status, such as: The arrears status, the lender’s financial position and solvency, assessment of the primary repayment source for the debt, status of the collateral, financial position of the guarantor, etc.

A debt is classified as impaired whenever the principal or interest thereof has been in arrears of 90 days or more, unless it is both well secured and under collection proceedings. Additionally, impaired debt is also considered as a debt whose terms were changed due to restructuring of troubled debt, unless a minimum loan loss provision was made in respect thereof before and after the restructuring according to the extent of arrears method.

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 specific debt examined and found to be delinquent for 90 days or more shall be classified as impaired, unless it is adequately secured and under collection proceedings.
- A debt examined on a collective basis 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;
  - Debt that is delinquent for 150 days or more will be fully accounted for as a provision and will undergo an accounting write-off;

Credit Exposures Delinquent for Over 90 Days Which are not Considered Impaired;

According to the directives of the Bank of Israel, in the situations outlined below, credit exposures delinquent for over 90 days which are not considered impaired;

- Credit that is assessed on a collective basis will be classified as “substandard” if it is delinquent for 90 days or more and will undergo an accounting write-off after being delinquent for 150 days.
- Housing loans for which the provision is calculated according to the depth of arrears.

Restructured Troubled Debt

A formal restructuring of a debt is considered a troubled debt restructuring if the Bank - for economic or legal reasons related to the debtor’s financial difficulties - granted a concession by changing the terms of the loan to alleviate the burden of the debtor’s near-term cash payments or by accepting other assets in satisfaction of the debt. In order to determine whether a debt restructuring carried out by the Bank constitutes restructuring of a troubled debt, the Bank carries out a qualitative assessment of the debt restructuring’s terms and circumstances with the aim of determining whether (1) the borrower has financial difficulties and (2) the Bank granted a concession to the borrower as part of the debt restructuring.

Differences Between the Definitions of Delinquency/Arrears and Failure for Accounting and Regulatory Purposes

Following are the differences between the definition of "arrears" or “delinquency” and “delinquent debt" or “debt in arrears” for accounting purposes and the definition of “loans in arrears" or “delinquent loans” for the purpose of measuring capital adequacy (regulatory purposes):

1. Debt is defined as “in arrears" or “delinquent” for accounting purposes after 30 days of arrears, while for capital adequacy purposes, “loans in arrears” or “delinquent loans” are defined as such only after having been in arrears/delinquent for 90 days;
2. A debt that has been restructured and classified as accruing interest, will be considered an “impaired” debt for accounting purposes, as long as it has not undergone "subsequent restructuring”, while for the purpose of measuring capital adequacy, it will not be considered a “loan in arrears” or “delinquent loan” (i.e., and be treated as "good" debt);
3. Off-balance sheet credit is classified as troubled debt if the materialization of the contingent liability is defined as “possible” and if the debts that may be recognized as a result of the materialization of the contingent liability may be classified as “troubled debt”. On the other hand, off-balance sheet credit exposures will be classified as delinquent for capital adequacy purposes consistently with the classification of the same borrower's balance sheet exposures.

For more information about the credit risk metrics, please see under “Credit Risks” in the Report of the Board of Directors and Management.

Impairment of Securities

For each reporting period, the Bank examines the need to record impairment losses for the securities in the available-for-sale portfolio and in the held-to-maturity portfolio, which are not temporary in nature. The assessment is made in case of indications that the securities may have been impaired. The criteria for determining whether or not the impairment is not of a temporary nature are set out in Note 1I to the Financial Statements.

Loan Loss Provision

A loan loss provision is made in accordance with one of the following methods:

- Specific provision - for debts over NIS 1 million classified as impaired and for any debt that has been restructured.
- Collective provision - for other debts that do not meet the abovementioned criteria for specific assessment with the exception of housing loans, which are treated according to the extent of arrears method.

For additional information, see Note 1H to the Financial Statements.

Credit Risk by Economic Sector

	December 31 2018									
	Total credit risk[(a)]			Debts[(b)] and off-balance sheet credit risk (net of derivatives)[(c)]						
								Loan losses[(d)]		
					[1]Of which:			Expenses (income) in respect of loan losses	Net accoun-ting write-offs	Balance of loan loss provision
	Total	Credit rating[(e)]	Trou-bled[(f)]	Total[1]	Debts[(b)]	Trou-bled[(f)]	Impaired			
	In NIS millions									
In respect of borrower activity in Israel										
Commercial public										
Agriculture	**2,102**	**2,015**	**87**	**2,101**	**1,786**	**87**	**42**	**(23)**	**(7)**	**(31)**
Mining and quarrying	**1,017**	**1,016**	**1**	**916**	**413**	**1**	**1**	**(2)**	**-**	**(1)**
Manufacturing	**24,314**	**23,457**	**857**	**23,935**	**15,805**	**857**	**470**	**9**	**(76)**	**(513)**
Construction & real estate - construction[(g)]	**47,469**	**46,704**	**765**	**47,316**	**21,906**	**765**	**282**	**7**	**10**	**(348)**
Construction & real estate - real estate activity	**28,665**	**28,061**	**604**	**28,554**	**25,413**	**604**	**433**	**(107)**	**(80)**	**(372)**
Power and water supply	**4,454**	**4,046**	**408**	**4,301**	**2,704**	**408**	**217**	**32**	**1**	**(86)**
Commerce	**29,556**	**28,465**	**1,091**	**29,442**	**24,880**	**1,090**	**277**	**129**	**131**	**(323)**
Hotels, accommodation and dining services	**3,232**	**3,149**	**83**	**3,218**	**2,795**	**83**	**62**	**46**	**1**	**(77)**
Transportation and storage	**8,187**	**7,828**	**359**	**8,124**	**6,406**	**359**	**69**	**36**	**28**	**(70)**
Information and communication	**5,389**	**5,318**	**71**	**5,189**	**3,669**	**71**	**23**	**(39)**	**(32)**	**(28)**
Financial services	**28,076**	**28,054**	**22**	**14,786**	**10,849**	**17**	**8**	**(13)**	**(6)**	**(185)**
Business and other services	**10,974**	**10,765**	**209**	**10,952**	**7,719**	**209**	**103**	**66**	**47**	**(172)**
Public and community services	**9,331**	**9,240**	**91**	**9,306**	**7,675**	**91**	**36**	**35**	**18**	**(79)**
Commercial - total[(h)]	**202,766**	**198,118**	**4,648**	**188,140**	**132,020**	**4,642**	**2,023**	**176**	**35**	**(2,285)**
Individuals - housing loans	**82,339**	**81,477**	**862**	**82,339**	**80,417**	**862**	**-**	**32**	**4**	**(473)**
Individuals - other	**64,930**	**63,951**	**979**	**64,925**	**36,320**	**979**	**383**	**241**	**165**	**(808)**
Less balances classified as held-for-sale assets[(i)]	**(19,869)**	**(19,497)**	**(372)**	**(19,869)**	**(8,210)**	**(372)**	**(45)**	**-**	**-**	**184**
Total loans to the public - activity in Israel	**330,166**	**324,049**	**6,117**	**315,535**	**240,547**	**6,111**	**2,361**	**449**	**204**	**(3,382)**
Banks in Israel	**4,287**	**4,287**	**-**	**2,716**	**2,703**	**-**	**-**	**-**	**-**	**(3)**
Less balances classified as held-for-sale assets[(i)]	**(33)**	**(33)**	**-**	**(33)**	**(33)**	**-**	**-**	**-**	**-**	**-**
Banks in Israel - total	**4,254**	**4,254**	**-**	**2,683**	**2,670**	**-**	**-**	**-**	**-**	**(3)**
Government of Israel	**39,916**	**39,916**	**-**	**74**	**74**	**-**	**-**	**-**	**-**	**-**
Total activity in Israel	**374,336**	**368,219**	**6,117**	**318,292**	**243,291**	**6,111**	**2,361**	**449**	**204**	**(3,385)**

(a) Balance-sheet credit risk and off-balance-sheet credit risk, including for derivatives. Including debt, bonds, securities borrowed or purchased under reverse repurchase agreements, 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 243,291, 39,193, 1,257, 7,985 and 82,610 million, respectively.

(b) Loans to the public, loans to governments, deposits with banks and other debt, excluding bonds and securities borrowed or purchased under reverse repurchase agreements.

(c) Credit risk for off-balance sheet financial instruments as calculated for the purpose of per borrower credit limitations, excluding for derivatives.

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

(e) Credit risk whose credit rating at the reporting date matches the credit rating for granting new credit in accordance with the Bank's policy.

(f) Balance-sheet and off-balance sheet credit risk that is impaired, substandard or under special supervision, including housing loans for which there is a provision according to the extent of arrears and housing loans for which there is no provision based on the extent of arrears which are in arrears of 90 days or more.

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

(h) The balance of outstanding commercial debts includes outstanding housing loans in the amount of NIS 913 million extended to purchasing groups currently in the process of construction.

(i) For more information regarding the investee's held-for-sale operations, please see the section entitled “Main Changes in the Reporting Period” in the Report of the Board of Directors and Management and Note 36F to the Financial Statements.

	December 31 2018									
	Total credit risk(a)			Debts(b) and off-balance sheet credit risk (net of derivatives)(c)						
								Loan losses(d)		
					1Of which:			Expenses (income) in respect of loan losses	Net accoun-ting write-offs	Balance of loan loss provision
	Total	Credit rating(e)	Trou-bled(f)	Total1	Debts(b)	Trou-bled(f)	Impaired			
	In NIS millions									
In respect of borrower activity abroad										
Commercial public										
Agriculture	**114**	**114**	**-**	**113**	**80**	**-**	**-**	**-**	**-**	**(1)**
Mining and quarrying	**76**	**76**	**-**	**76**	**-**	**-**	**-**	**-**	**-**	**-**
Manufacturing	**7,649**	**7,491**	**158**	**5,924**	**3,875**	**158**	**69**	**54**	**49**	**(42)**
Construction and real estate(g)	**15,667**	**14,637**	**1,030**	**15,190**	**12,003**	**1,030**	**385**	**2**	**(23)**	**(212)**
Power and water supply	**272**	**272**	**-**	**68**	**9**	**-**	**-**	**-**	**-**	**-**
Commerce	**6,521**	**6,338**	**183**	**6,206**	**4,362**	**183**	**78**	**16**	**23**	**(48)**
Hotels, accommodation and dining services	**2,226**	**2,226**	**-**	**2,211**	**2,128**	**-**	**-**	**(7)**	**-**	**(10)**
Transportation and storage	**286**	**283**	**3**	**203**	**190**	**3**	**3**	**7**	**6**	**(3)**
Information and communication	**2,800**	**2,709**	**91**	**1,873**	**1,084**	**91**	**32**	**6**	**3**	**(30)**
Financial services	**19,936**	**19,920**	**16**	**4,344**	**3,412**	**16**	**16**	**(7)**	**(5)**	**(25)**
Business and other services	**7,650**	**7,611**	**39**	**6,146**	**5,416**	**39**	**-**	**1**	**(2)**	**(49)**
Public and community services	**517**	**517**	**-**	**515**	**359**	**-**	**-**	**(1)**	**-**	**(3)**
Commercial - total	**63,714**	**62,194**	**1,520**	**42,869**	**32,918**	**1,520**	**583**	**71**	**51**	**(423)**
Individuals - housing loans	**474**	**443**	**31**	**473**	**473**	**31**	**31**	**-**	**-**	**(6)**
Individuals - other	**657**	**640**	**17**	**657**	**587**	**17**	**2**	**(1)**	**1**	**(2)**
Total loans to the public - overseas activity	**64,845**	**63,277**	**1,568**	**43,999**	**33,978**	**1,568**	**616**	**70**	**52**	**(431)**
Foreign banks	**31,712**	**31,712**	**-**	**13,173**	**12,279**	**-**	**-**	**-**	**-**	**-**
Less balances classified as held-for-sale assets(h)	**(2)**	**(2)**	**-**	**(2)**	**(2)**	**-**	**-**	**-**	**-**	**-**
Foreign banks - total	**31,710**	**31,710**	**-**	**13,171**	**12,277**	**-**	**-**	**-**	**-**	**-**
Foreign governments	**6,977**	**6,977**	**-**	**1,020**	**708**	**-**	**-**	**-**	**-**	**-**
Total activity abroad	**103,532**	**101,964**	**1,568**	**58,190**	**46,963**	**1,568**	**616**	**70**	**52**	**(431)**
Total	**477,868**	**470,183**	**7,685**	**376,482**	**290,254**	**7,679**	**2,977**	**519**	**256**	**(3,816)**

(a) Balance-sheet credit risk and off-balance-sheet credit risk, including for derivatives. Including debt, bonds, 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 46,963, 31,820, -, 4,771 and 19,978 million, respectively.

(b) Loans to the public, loans to governments, deposits with banks and other debt, excluding bonds and securities borrowed or purchased under reverse repurchase agreements.

(c) Credit risk for off-balance sheet financial instruments as calculated for the purpose of per borrower credit limitations, excluding for derivatives.

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

(e) Credit risk whose credit rating at the reporting date matches the credit rating for granting new credit in accordance with the Bank's policy.

(f) Balance-sheet and off-balance sheet credit risk that is impaired, substandard or under special supervision, including housing loans for which there is a provision according to the extent of arrears and housing loans for which there is no provision based on the extent of arrears which are in arrears of 90 days or more.

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

(h) For more information regarding the investee's held-for-sale operations, please see the section entitled “Main Changes in the Reporting Period” in the Report of the Board of Directors and Management and Note 36F to the Financial Statements.

	December 31 2017									
	Total credit risk[a]			Debts[b] and off-balance sheet credit risk (net of derivatives)[c]						
								Loan losses[d]		
					[1]Of which:					
	Total	Credit rating[e]	Trou-bled[f]	Total[1]	Debts[b]	Trou-bled[f]	Impaired	Expenses (income) in respect of loan losses	Net accoun-ting write-offs	Balance of loan loss provision
	In NIS millions									
In respect of borrower activity in Israel										
Commercial public										
Agriculture	2,151	1,993	158	2,150	1,850	157	70	9	2	(61)
Mining and quarrying	984	983	1	957	539	1	-	-	-	(1)
Manufacturing	23,011	21,998	1,013	22,778	14,963	1,009	577	104	148	(472)
Construction & real estate - construction[g]	49,881	48,679	1,202	49,820	19,128	1,202	309	72	47	(354)
Construction & real estate - real estate activity	27,695	26,941	754	27,611	24,438	754	672	(302)	(252)	(399)
Power and water supply	4,299	3,954	345	4,219	2,838	345	237	(7)	6	(55)
Commerce	27,937	26,973	964	27,809	23,162	719	335	57	87	(309)
Hotels, accommodation and dining services	3,323	3,161	162	3,297	2,844	162	59	(6)	(8)	(29)
Transportation and storage	8,255	7,797	458	8,194	6,887	451	250	38	22	(64)
Information and communication	5,260	5,198	62	5,055	3,673	61	50	(28)	3	(38)
Financial services	21,720	21,706	14	14,021	11,189	8	3	(76)	(56)	(145)
Business and other services	10,603	10,466	137	10,577	7,791	137	56	42	40	(154)
Public and community services	9,453	9,391	62	9,439	7,969	62	19	28	22	(62)
Commercial - total[h]	194,572	189,240	5,332	185,927	127,271	5,068	2,637	(69)	61	(2,143)
Individuals - housing loans	79,034	78,313	721	79,034	77,448	984	-	(10)	8	(443)
Individuals - other	66,476	65,535	941	66,470	36,222	933	372	188	229	(733)
Total loans to the public - activity in Israel[i]	340,082	333,088	6,994	331,431	240,941	6,985	3,009	109	298	(3,319)
Banks in Israel	3,921	3,921	-	1,701	1,650	-	-	2	-	(3)
Government of Israel	41,161	41,161	-	129	129	-	-	-	-	-
Total activity in Israel	385,164	378,170	6,994	333,261	242,720	6,985	3,009	111	298	(3,322)

(a) Balance-sheet credit risk and off-balance-sheet credit risk, including for derivatives. Including debt, bonds, 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 242,720, 40,102, 1,161, 3,286 and 97,895 million, respectively.

(b) Loans to the public, loans to governments, deposits with banks and other debt, excluding bonds and securities borrowed or purchased under reverse repurchase agreements.

(c) Credit risk for off-balance sheet financial instruments as calculated for the purpose of per borrower credit limitations, excluding for derivatives.

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

(e) Credit risk whose credit rating at the reporting date matches the credit rating for granting new credit in accordance with the Bank's policy.

(f) Balance-sheet and off-balance sheet credit risk that is impaired, substandard or under special supervision, including housing loans for which there is a provision according to the extent of arrears and housing loans for which there is no provision based on the extent of arrears which are in arrears of 90 days or more.

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

(h) 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.

(i) The figures were reclassified following an improvement process performed in 2018.

	December 31 2017									
	Total credit risk[a]			Debts[b] and off-balance sheet credit risk (net of derivatives)[c]						
								Loan losses[d]		
					[1]Of which:			Expenses (income) in respect of loan losses	Net accounting write-offs	Balance of loan loss provision
	Total	Credit rating[e]	Troubled[f]	Total[1]	Debts[b]	Troubled[f]	Impaired			
	In NIS millions									
In respect of borrower activity abroad										
Commercial public										
Agriculture	100	100	-	98	60	-	-	-	-	(1)
Mining and quarrying	35	35	-	35	30	-	-	-	-	-
Manufacturing	7,564	7,249	315	6,420	4,567	315	78	(5)	5	(32)
Construction and real estate[g]	14,223	13,313	910	13,496	9,748	910	431	19	80	(136)
Power and water supply	260	260	-	87	22	-	-	-	-	-
Commerce	6,371	6,165	206	6,203	4,406	206	34	19	3	(71)
Hotels, accommodation and dining services	2,250	2,250	-	2,234	2,056	-	-	5	1	(15)
Transportation and storage	84	63	21	67	50	21	21	18	8	(15)
Information and communication	1,829	1,771	58	1,596	875	58	21	8	-	(9)
Financial services	16,071	15,992	79	2,135	1,527	79	79	(5)	1	(43)
Business and other services	6,430	6,429	1	6,160	5,411	1	1	6	15	(28)
Public and community services	627	617	10	618	441	10	-	-	-	(17)
Commercial - total	55,844	54,244	1,600	39,149	29,193	1,600	665	65	113	(367)
Individuals - housing loans	510	480	30	509	509	30	29	(3)	1	(7)
Individuals - other	608	603	5	608	522	5	5	(1)	-	(4)
Total loans to the public - overseas activity	56,962	55,327	1,635	40,266	30,224	1,635	699	61	114	(378)
Foreign banks	31,247	31,247	-	11,251	10,214	-	-	-	-	-
Foreign governments	12,047	12,047	-	1,210	586	-	-	-	-	-
Total activity abroad	100,256	98,621	1,635	52,727	41,024	1,635	699	61	114	(378)
Total	485,420	476,791	8,629	385,988	283,744	8,620	3,708	172	412	(3,700)

(a) Balance-sheet credit risk and off-balance-sheet credit risk, including for derivatives. Including debt, bonds, 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 41,024, 32,963, -, 6,294 and 19,975 million, respectively.

(b) Loans to the public, loans to governments, deposits with banks and other debt, excluding bonds and securities borrowed or purchased under reverse repurchase agreements.

(c) Credit risk for off-balance sheet financial instruments as calculated for the purpose of per borrower credit limitations, excluding for derivatives.

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

(e) Credit risk whose credit rating at the reporting date matches the credit rating for granting new credit in accordance with the Bank's policy.

(f) Balance-sheet and off-balance sheet credit risk that is impaired, substandard or under special supervision, including housing loans for which there is a provision according to the extent of arrears and housing loans for which there is no provision based on the extent of arrears which are in arrears of 90 days or more.

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

Credit Exposures by Remaining Loan Term[a]

	December 31 2018				
	Up to one year	From one to five years	Over five years	Without loan term	Total credit exposure
	In NIS millions				
Balance-sheet credit exposure:					
Commercial	**95,381**	**62,155**	**34,218**	**3,723**	**195,477**
Individuals - housing loans	**7,571**	**25,690**	**78,296**	**154**	**111,711**
Individuals - other	**18,204**	**20,920**	**1,602**	**559**	**41,285**
Assets in respect of derivatives	**7,621**	**939**	**281**	**-**	**8,841**
Total - public	**128,777**	**109,704**	**114,397**	**4,436**	**357,314**
Banks and governments[b]	**99,278**	**24,007**	**13,797**	**-**	**137,082**
Total balance-sheet credit exposure	**228,055**	**133,711**	**128,194**	**4,436**	**494,396**
Of which: Bonds	**27,846**	**24,215**	**27,324**	**-**	**79,385**
Total off balance-sheet credit risk exposure	**71,980**	**49,850**	**5,838**	**-**	**127,668**

	December 31 2017				
	Up to one year	From one to five years	Over five years	Without loan term	Total credit exposure
	In NIS millions				
Balance-sheet credit exposure:					
Commercial	88,781	57,799	29,942	3,744	180,266
Individuals - housing loans	6,652	24,358	71,879	159	103,048
Individuals - other	16,930	19,346	1,763	431	38,470
Assets in respect of derivatives	1,675	1,345	51	-	3,071
Total - public	114,038	102,848	103,635	4,334	324,855
Banks and governments[b]	118,955	18,785	12,110	2	149,852
Total balance-sheet credit exposure	232,993	121,633	115,745	4,336	474,707
Of which: Bonds	38,037	17,196	22,526	-	77,759
Total off balance-sheet credit risk exposure	70,213	50,865	4,269	-	125,347

(a) The amounts represent expected future cash flows based on the remaining contractual term of each cash flow for balance-sheet credit risk and off-balance sheet credit risk (excluding off-balance sheet credit risk arising from derivative instruments).
(b) Including bonds of banks and governments and assets for derivatives against banks.

Exposure to Foreign Countries[a]

Part A - Information regarding total exposure to foreign countries and exposures to countries where the total exposure to each country is more than 1 percent of total consolidated assets or more than 20 percent of total capital, whichever is lower:

	1	2	3	4	5	4-5=6
	December 31 2018					
	Balance sheet exposure[b]					
Country	Cross-border balance sheet exposure			Balance sheet exposure of the banking corporation's foreign offices to the local residents of that foreign country		
	To governments[d]	To banks	To others	Balance sheet exposure before deduction of local liabilities	Deduction for local liabilities	Net balance sheet exposure after deduction of local liabilities
	In NIS millions					
United States	**6,518**	**4,667**	**11,408**	**25,117**	**13,506**	**11,611**
United Kingdom	**-**	**4,755**	**2,182**	**5,988**	**2,030**	**3,958**
France	**1,127**	**1,431**	**236**	**-**	**-**	**-**
Switzerland	**-**	**804**	**423**	**23**	**23**	**-**
Germany	**3,830**	**358**	**263**	**-**	**-**	**-**
Other	**2,418**	**6,826**	**5,900**	**1,087**	**575**	**512**
Total exposures to foreign countries	**13,893**	**18,841**	**20,412**	**32,215**	**16,134**	**16,081**
Total exposures to LDCs	**706**	**1,282**	**1,398**	**1,076**	**570**	**506**
Total exposures to the GIPS countries	**253**	**137**	**65**	**-**	**-**	**-**

	1	2	3	4	5	4-5=6
	December 31 2017					
	Balance sheet exposure[b]					
Country	Cross-border balance sheet exposure			Balance sheet exposure of the banking corporation's foreign offices to the local residents of that foreign country		
	To governments[d]	To banks	To others	Balance sheet exposure before deduction of local liabilities	Deduction for local liabilities	Net balance sheet exposure after deduction of local liabilities
	In NIS millions					
United States	10,463	1,461	8,168	23,080	12,345	10,735
United Kingdom	503	4,640	2,572	6,031	1,729	4,302
France	1,624	1,012	210	-	-	-
Switzerland	92	710	554	44	41	3
Germany	3,204	80	674	-	-	-
Other	996	7,994	5,390	1,077	544	533
Total exposures to foreign countries[e]	16,882	15,897	17,568	30,232	14,659	15,573
Total exposures to LDCs[f]	237	1,201	1,172	1,065	543	522
Total exposures to the GIPS countries[g]	470	74	231	-	-	-

Please see comments above.

6+3+2+1=7	8	9	10	11	12	13
			Off-balance sheet exposure(b)(c)		Cross-border balance sheet exposure(b)	
Total balance sheet exposure						
	Troubled balance-sheet credit risk	Impaired debts	Total off balance-sheet exposure	Of which: Off balance-sheet troubled credit risk	Loan term: up to one year	Loan term: over one year
34,204	**976**	**435**	**6,704**	**-**	**10,485**	**12,108**
10,895	**183**	**115**	**6,983**	**80**	**3,909**	**3,028**
2,794	**18**	**7**	**1,654**	**-**	**1,938**	**856**
1,227	**80**	**-**	**1,064**	**-**	**636**	**591**
4,451	**47**	**-**	**1,086**	**-**	**743**	**3,708**
15,656	**80**	**73**	**2,646**	**-**	**5,627**	**9,517**
69,227	**1,384**	**630**	**20,137**	**80**	**23,338**	**29,808**
3,892	**68**	**68**	**1,418**	**-**	**513**	**2,873**
455	**7**	**-**	**221**	**-**	**64**	**391**

6+3+2+1=7	8	9	10	11	12	13
			Off-balance sheet exposure(b)(c)		Cross-border balance sheet exposure(b)	
Total balance sheet exposure						
	Troubled balance-sheet credit risk	Impaired debts	Total off balance-sheet exposure	Of which: Off balance-sheet troubled credit risk	Loan term: up to one year	Loan term: over one year
30,827	1,190	418	5,838	-	6,667	13,425
12,017	160	160	7,513	-	4,395	3,320
2,846	13	12	1,968	-	1,551	1,295
1,359	-	-	1,898	-	766	590
3,958	-	-	2,208	-	2,211	1,747
14,913	117	111	2,850	-	7,043	7,337
65,920	1,480	701	22,275	-	22,633	27,714
3,132	96	93	1,935	-	393	2,217
775	-	-	234	-	659	116

Comments:

(a) Exposure to foreign countries is presented based on the final risk.
(b) Balance-sheet and off-balance-sheet credit risk, troubled commercial credit risk and impaired debts are stated before the effect of the provision for loan losses and the effect of collateral that is deductible for the purpose of specific and general indebtedness and before the effect of netting in respect of derivatives..
(c) Credit risk for off-balance sheet financial instruments as calculated for the purpose of per borrower credit limitations, before the effect of netting in respect of derivatives.
(d) Governments, public institutions, and central banks.
(e) In 2018, including balances classified as held for sale assets in the amount of NIS 1.3 million.
(f) “Exposure to LDCs” includes total exposure to countries defined as least developed countries (LDCs), which are classified by the World Bank as low or mid-income countries.
(g) “Exposure to the GIPS countries” includes: Greece, Italy, Portugal and Spain.

Part B - As at December 31 2018 and December 31 2017, there is no aggregate balance sheet exposure to foreign countries, the total exposure to each of which ranges between 0.75 percent and 1 percent of total consolidated assets or between 15 percent and 20 percent of capital, whichever the lower.

Part C - The total exposure amount to foreign countries with liquidity issues as defined by the Bank of Israel (a country receiving financial support from the International Monetary Fund or whose liabilities are rated CCC or lower), as of December 31 2018, amounts to NIS 731 million in respect of 12 countries (as at December 31 2017 - NIS 610 million, in respect of 9 countries).

For more information regarding movement in the loan loss provision, please see Notes 13 and 30 to the Financial Statements.
For more information regarding aging of delinquent credit exposures, please see Note 30 to the Financial Statements.
For more information regarding restructured credit exposures, please see Note 30 to the Financial Statements and the “Credit Risks” section in the Report of the Board of Directors and Management.

Credit Risk Mitigation

Credit Risk Mitigation Techniques (CRC)

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

As part of its collateral policy for all economic sectors, the Bank has set principles and rules regarding collateral types and amounts. The collateral requirements and rates are in line with 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 treatment, methods and timing for updating its value and means of control and monitoring.

As far as possible, collateral are adapted to the kind of credit they secure, taking into account the time frame, types of linkage, nature and purpose of the credit, as well as the speed at which the collateral can be realized. The Bank verifies the value of the main collateral (particularly in the real estate and equipment sectors) 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 system which can generate information regarding the type of assets used as collateral.

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

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

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

Among other things, the Bank uses netting letters that constitute qualified collateral under Proper Conduct of Banking Business Directive No. 203 for calculating capital adequacy.

The Bank uses qualified collateral to change the risk weighting of debts backed by guarantees to the risk weight of the security provider, when calculating the risk assets under the standardized approach. For this purpose, the Bank recognizes mainly the following types of collateral as valid: guarantees and insurance policies of the Israeli Government and of Israeli banks, as well as of other high-rated credit granting entities and insurers, which meet the validity criteria for capital adequacy purposes

Credit Risk Mitigation Techniques – Overview (CR3)

		A	A1	A2	B	C	D	E
		December 31 2018						
		Unsec-ured	Secured[c]					
					Of which: by collateral		Of which: by financial guarantees	
		Carrying value[a]	Carrying value[a]	Of which: secured amount[b]	Carrying value[a]	Of which: secured amount[b]	Carrying value[a]	Of which: secured amount[b]
		In NIS millions						
1	Debts, excluding bonds	**272,210**	**22,766**	**8,973**	**18,950**	**6,382**	**3,816**	**2,591**
2	Bonds	**45,280**	**7,943**	**7,943**	**-**	**-**	**7,943**	**7,943**
3	Total	**317,490**	**30,709**	**16,916**	**18,950**	**6,382**	**11,759**	**10,534**
4	Of which: Impaired or in arrears of 90 days or more	**3,682**	**176**	**129**	**130**	**88**	**46**	**41**

		A	A1	A2	B	C	D	E
		December 31 2017						
		Unsec-ured	Secured[c]					
					Of which: by collateral		Of which: by financial guarantees	
		Carrying value[a]	Carrying value[a]	Of which: secured amount[b]	Carrying value[a]	Of which: secured amount[b]	Carrying value[a]	Of which: secured amount[b]
		In NIS millions						
1	Debts, excluding bonds	257,425	23,103	8,197	20,229	6,195	2,874	2,002
2	Bonds	53,600	6,387	6,387	-	-	6,387	6,387
3	Total	311,025	29,490	14,584	20,229	6,195	9,261	8,389
4	Of which: Impaired or in arrears of 90 days or more	4,257	91	16	87	16	4	-

(a) Carrying value according to the accounting values reported in the financial statements and after other than temporary provisions for loan losses or impairments.

(b) Carrying value of the share of the debts secured by collateral, guarantees or credit derivative, after taking into account precautionary measures.

(c) Carrying value of said debts, after other than temporary provisions for loan losses or impairments, partially or fully secured, regardless of the specific portion secured for the original exposure.

Standardized Approach for Credit Risk

Use of External Credit Ratings under the Standardized Approach for Credit Risk

The credit risk exposures is weighted according to the standardized approach. Under this approach, risk weights 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

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, as updated in 2018.

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 weight. When there are two ratings, by two different agencies, mapped for different risk weights, the higher risk weight is selected. When three ratings are available, the best two ratings will be taken into account, and from these, the risk weight referring to the lower rating of the two will be selected.

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 three rating agencies.

Standardized Approach – Credit Risk Exposure and Credit Risk Mitigation Effects (CR4)

		A	B	C	D	E	F
		December 31 2018					
		Exposures before CCF and CRM		Exposures after CCF and CRM		RWA and RWA density	
	Asset classes	Balance sheet amount(b)	Off-balance sheet amount(b)	Balance sheet amount(c)	Off-balance sheet amount(b)	RWA	RWA density
		In NIS millions					
1	Sovereignties, their central banks and national monetary authority	**105,287**	**347**	**113,565**	**304**	**1,846**	**1.62%**
2	Public sector entities (PSEs) other than a central government	**17,535**	**1,747**	**11,737**	**616**	**3,634**	**29.42%**
3	Banks, including multilateral development banks (MDBs)	**18,213**	**4,211**	**17,008**	**1,921**	**3,971**	**20.98%**
4	Securities firms	**2,408**	**-**	**2,408**	**-**	**482**	**20.00%**
5	Corporations	**94,385**	**42,694**	**90,367**	**16,731**	**101,051**	**94.35%**
6	Retail exposures to individuals	**42,759**	**30,245**	**42,096**	**4,061**	**34,618**	**75.00%**
7	Loans to small businesses	**17,542**	**5,119**	**16,060**	**1,180**	**12,930**	**75.00%**
8	Secured by a residential property	**79,375**	**5,812**	**79,327**	**817**	**44,294**	**55.27%**
9	Secured by a commercial property	**40,365**	**38,152**	**39,941**	**13,159**	**53,100**	**100.00%**
10	Delinquent loans(1)		**3,640**		**3,263**	**4,308**	**132.02%**
11	Other assets	**12,080**	**-**	**12,080**	**-**	**9,802**	**81.14%**
12	Total	**433,589**	**128,327**	**427,852**	**38,789**	**270,036**	**57.87%**

		A	B	C	D	E	F
		December 31 2017					
		Exposures before CCF and CRM		Exposures after CCF and CRM		RWA and RWA density	
	Asset classes	Balance sheet amount(b)	Off-balance sheet amount(b)	Balance sheet amount(c)	Off-balance sheet amount(b)	RWA	RWA density
		In NIS millions					
1	Sovereignties, their central banks and national monetary authority	117,761	619	124,636	832	1,746	1.39%
2	Public sector entities (PSEs) other than a central government	14,514	1,148	10,120	440	3,460	32.77%
3	Banks, including multilateral development banks (MDBs)	15,399	4,321	14,458	2,010	3,217	19.54%
4	Securities firms	739	-	739	-	148	20.03%
5	Corporations	87,916	41,525	83,829	16,758	91,727	91.19%
6	Retail exposures to individuals	43,814	30,973	42,980	4,090	35,303	75.00%
7	Loans to small businesses	18,084	5,103	16,533	1,179	13,284	75.00%
8	Secured by a residential property	76,553	4,453	76,514	546	42,848	55.60%
9	Secured by a commercial property	36,003	37,824	35,549	18,554	54,103	100.00%
10	Delinquent loans(d)		3,038		3,010	4,061	134.92%
11	Other assets	13,224	-	13,224	-	9,976	75.44%
12	Total	427,045	125,966	421,592	44,409	259,873	55.77%

(a) The balances in the disclosure include balance sheet and off-balance sheet balances reflecting credit risk, excluding deferred tax amounts and investments in financial corporations below the deduction thresholds (subject to a 250 percent risk weight), counterparty credit risk exposures (included in Part 5A to the Report), and securitization (included in Appendix B to this report).

(b) The balances reflect the regulatory exposure amounts, net of provisions and write-offs, before credit conversion coefficients and before credit risk mitigation methods.

(c) The balances reflect the regulatory exposure amounts, net of provisions and write-offs, after credit conversion coefficients and after credit risk mitigation methods.

(d) Balance sheets and off-balance sheets balances were merged due to immateriality.

Standardized Approach – Exposures by Asset Classes and Risk Weights[a][b] (CR5)

		A	C	D	E	F		G	H	I	M
		December 31 2018									
	Asset classes / risk weight	0%	10%	20%	35%	50%	60%	75%	100%	150%	Total credit exposures amount (after CCF and CRM)
		In NIS millions									
1	Sovereignties, their central banks and national monetary authority	**106,375**	**-**	**6,656**	**-**	**646**	**-**	**-**	**192**	**-**	**113,869**
2	Public sector entities (PSEs) other than a central government	**1,961**	**-**	**5,216**	**-**	**5,172**	**-**	**-**	**4**	**-**	**12,353**
3	Banks, including multilateral development banks (MDBs)	**2,417**	**-**	**15,024**	**-**	**1,035**	**-**	**-**	**453**	**-**	**18,929**
4	Securities firms	**-**	**-**	**2,408**	**-**	**-**	**-**	**-**	**-**	**-**	**2,408**
5	Corporations	**-**	**-**	**7,295**	**-**	**751**	**-**	**-**	**98,733**	**319**	**107,098**
6	Retail exposures to individuals	**-**	**-**	**-**	**-**	**-**	**-**	**46,157**	**-**	**-**	**46,157**
7	Loans to small businesses	**-**	**-**	**-**	**-**	**-**	**-**	**17,240**	**-**	**-**	**17,240**
8	Secured by a residential property	**-**	**-**	**-**	**28,493**	**17,874**	**3,398**	**28,132**	**2,247**	**-**	**80,144**
9	Secured by a commercial property	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**53,100**	**-**	**53,100**
10	Delinquent loans	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**1,172**	**2,091**	**3,263**
11	Other assets	**2,597**	**-**	**-**	**-**	**-**	**-**	**-**	**8,844**	**639**	**12,080**
11A	Of which: for shares	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**3,897**	**639**	**4,536**
12	Total	**113,350**	**-**	**36,599**	**28,493**	**25,478**	**3,398**	**91,529**	**164,745**	**3,049**	**466,641**

	Asset classes / risk weight	A	C	D	E	F		G	H	I	M
		December 31 2017									
		0%	10%	20%	35%	50%	60%	75%	100%	150%	Total credit exposures amount (after CCF and CRM)
		In NIS millions									
1	Sovereignties, their central banks and national monetary authority	119,695	-	4,581	-	727	-	-	466	-	125,469
2	Public sector entities (PSEs) other than a central government	1,527	-	3,537	-	5,487	-	-	9	-	10,560
3	Banks, including multilateral development banks (MDBs)	3,622	-	11,475	-	897	-	-	472	2	16,468
4	Securities firms	-	-	739	-	-	-	-	-	-	739
5	Corporations	-	-	9,937	-	2,042	-	-	88,387	220	100,586
6	Retail exposures to individuals	-	-	-	-	-	-	47,070	-	-	47,070
7	Loans to small businesses	-	-	-	-	-	-	17,712	-	-	17,712
8	Secured by a residential property	-	-	-	28,984	15,611	-	30,269	2,196	-	77,060
9	Secured by a commercial property	-	-	-	-	-	-	-	54,103	-	54,103
10	Delinquent loans	-	-	-	-	-	-	-	906	2,104	3,010
11	Other assets	3,539	-	-	-	-	-	-	9,102	583	13,224
11A	Of which: for shares	-	-	-	-	-	-	-	3,265	583	3,848
12	Total	128,383	-	30,269	28,984	24,764	-	95,051	155,641	2,909	466,001

(a) The balances in the disclosure include balance sheet and off-balance sheet balances reflecting credit risk, excluding deferred tax amounts and investments in financial corporations below the deduction thresholds (subject to a 250 percent risk weight), counterparty credit risk exposures (included in Part 5A to the Report), and securitization (included in Appendix B to this report).

(b) The balances reflect the regulatory exposure amounts, net of provisions and write-offs, after credit conversion coefficients and after credit risk mitigation methods.

Additional Information about Credit Risk

Activity and Risk Boundaries in the Construction and Real Estate Industry

The construction and real estate industry is the area of activity to which the Bank has the greatest exposure of all the business economic sectors. As with other economic sectors, the credit policy outlines internal methodologies and criteria for financing transactions for each of the real estate industry's sub-sectors.

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 tracking the development of the segment'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.

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.

Further to similar policies purchased in the past, in 2018, an insurance policy was purchased for the portfolio of guarantees under the Sale (Apartments) Law and for the commitment to issue guarantees from global insurers with high credit global ratings. 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 enables the Bank to reduce its held capital in respect of the credit risk arising from the issuance of the guarantees, using the policy as a "credit risk mitigator" (the deduction is in line with the reinsurers' ratings). The insurance is for projects which commenced by December 31 2019. As of December 31 2018, 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.

Development of Indebtedness for the Construction and Real Estate Industry (in Israel and Overseas)

	December 31		Change	
	2018	2017		
	In NIS millions		In NIS millions	In %
Balance-sheet credit risk	**59,954**	54,048	5,906	10.9
Guarantees for apartment buyers[a]	**4,655**	8,082	(3,427)	(42.4)
Other off-balance sheet credit risk[a]	**27,192**	29,669	(2,477)	(8.3)
Total credit risk	**91,801**	91,799	2	-

(a) In credit risk terms.

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

Housing Loan Portfolio Risks

Economic developments in Israel in recent years (a low interest environment, results of the affordable housing plans, and the stabilization of high housing prices) have led to a significant increase in housing credit provision in Israel.
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 rates, and LTV ratio.

Development of Total Outstanding Housing Loans in Israel, Net

	Outstanding loans portfolio	Change from end of previous year
	In NIS millions	In %
December 31 2016	78,184	(2.4)
December 31 2017	77,005	(1.5)
December 31 2018	**79,944**	**3.8**

In 2018, there was an increase in the volume of housing loans as a result of an increase in the number of loans granted in response to growing demand for credit alongside and the termination of the Bank’s agreement with an institutional body for joint loan granting in early 2018, which was not renewed.

As part of its monitoring of risk centers in the housing loan portfolio, the Bank also monitors characteristics of the portfolio and characteristics of the new credit, including the new credit’s distribution by LTV ratios and repayment ratios (the Loan-to-value ratio is the ratio between the total credit approved for the borrower - even if it has not yet been extended in effect, either in full or in part - and the value of the mortgaged property during the approval of the credit line. The repayment ratio is the portion of the monthly repayment out of the borrower's disposable monthly income).

Development of New Outstanding Loans Granted in Israel at a Loan-To-Value Ratio of Over 60 Percent

	2018				2017	2016
	Q4	Q3	Q2	Q1	Annual average	Annual average
LTV ratio	In %[a]					
Over 60 to 70, inclusive	**17.2**	16.7	18.0	18.0	18.0	16.1
Over 70 to 80, inclusive	**16.1**	16.6	16.3	13.0	16.0	14.7
Over 80	**0.20**	0.07	0.05	0.20	0.09	0.12

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

For more information about this segment, please see under “Credit Risks” 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 highly diverse borrowers and a wide variety of credit products (various types of loans, current accounts, credit cards) at a lower scale (on average) of 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 a key 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/her 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 the Bank extended and boosted its ongoing monitoring of its entire consumer credit portfolio, while adhering to strict underwriting processes and management and control at the individual borrower level.

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

Groups of Borrowers

On August 1 2018, the Bank of Israel issued an amendment to Proper Conduct of Banking Business Directive No. 313 ("Restrictions on the Indebtedness of a Borrower or Group of Borrowers"): According to the amendment, a bank's exposure to a "credit card company type group of borrowers" shall not exceed 15 percent of the banking corporation's share capital, similarly to the restriction applicable to the exposure to a "banking borrower group." The Directive will become effective gradually, within 3 years of a credit company's split from the banking corporation.

For more information about borrower groups, please see under "Credit Risks" in the Report of the Board of Directors and Management.

Part 5 - Counterparty Credit Risk

Counterparty Credit Risk (CCRA)

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 expected volatility of the transaction's underlying asset and the period remaining until the completion of the collateral as agreed with the counterparty, after deducting enforceable netting agreements, as follows:

In the (marketable and over the counter) derivative market, Leumi implements mechanisms for credit risk mitigation of transactions between counterparties through netting mechanisms based on standard global legal agreements as well as on a the Credit Support Annex (CSA) mechanism between counterparties to a transaction, whether by containing exposure or through deeds of pledge. During the defined periods, netting is performed on a regular basis, according to the market data and exposure. The collateral is usually in cash, in the currencies agreed upon. Following are the types of such agreements currently in place at Leumi:

1. In over the counter (OTC) derivatives operations, the offsetting mechanisms are based on a standard international agreement infrastructure or a local agreement infrastructure that complies with international standards, as well as netting arrangements for the purpose of exposure containment, all in accordance with the provisions of the Transactions in Financial Assets Law. Thus, for example, the Bank enters into ISDA and CSA agreements with international parties and local customers active in the capital market. In addition, with a view to reducing counterparty risk, there is a major shift towards central clearing for interest rate derivatives in major currencies. As part of the ISDA agreements to which Bank Leumi is party, there is currently no correlation between a lowering of Leumi's credit rating and changing the collateral amount.
2. In activities in tradable derivatives abroad, the offsetting and netting mechanisms are based on agreements consistent with the provisions of the Transactions in Financial Assets Law.
3. In the local activity with MAOF (marketable derivatives), there are no specific netting agreements and the activity is performed against deeds of pledge or solo.

Credit facilities for customers' activity are set by individual credit committees in accordance with the Bank's credit policy, subject to the restrictions imposed by the Board of Directors. The considerations affecting the credit facility amount include, inter alia, credit risk analysis and business profile, including the collateral offered as backup for the credit arising from the activity.

The facilities for countries, banks and financial institutions are set by a dedicated committee with the participation of representatives from the relevant divisions, subject to the restrictions set in the Group's investment policy and market risk management.

The Bank's Capital Markets Division monitors counterparty credit exposures in all types of derivatives transactions. The Division closely monitors customers who are active in the financial and capital markets, as well as similar 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.

The Risk Management Division serves as a second line of defense, recommends to the Board of Directors the risk management policy, is responsible for reporting the exposures to the Board, and is responsible for validating the models and criteria employed to manage the risk.

Analysis of Counterparty Credit Risk (CCR) Exposure by Regulatory Approach (CCR1)

		A	B	E	F
		December 31 2018			
		Replacement cost	Potential future exposure	EAD after CRM	RWA
		In NIS millions			
1	Current exposure method	**6,254**	**10,722**	**8,144**	**4,228**
3	The comprehensive approach to credit risk mitigation (for securities financing transactions)	**-**	**-**	**1,257**	**-**
6	Total	**6,254**	**10,722**	**9,401**	**4,228**

		A	B	E	F
		December 31 2017			
		Replacement cost	Potential future exposure	EAD after CRM	RWA
		In NIS millions			
1	Current exposure method	3,261	9,668	8,177	3,108
3	The comprehensive approach to credit risk mitigation (for securities financing transactions)	-	-	1,161	-
6	Total	3,261	9,668	9,338	3,108

Credit Valuation Adjustment (CVA) Capital Charge (CCR2)

	A	B	A	B
	December 31			
		2018		2017
	EAD after CRM	RWA	EAD after CRM	RWA
	In NIS millions			
Total portfolios for which CVA is calculated according to the standardized approach	**7,857**	**1,518**	8,171	1,674

Standardized Approach of Counterparty Credit Risk (CCR) Exposures by Regulatory Portfolio and Risk Weights[(a)] (CCR3)

	A	B	C	D	E	F	G	H	I
	December 31 2018								
Regulatory portfolio / risk weight	0%	10%	20%	50%	75%	100%	150%	Other	Total credit exposure
	In NIS millions								
Sovereignties	**1,275**	**-**	**-**	**-**	**-**	**11**	**-**	**-**	**1,286**
Public sector entities (PSEs) other than a central government	**-**	**-**	**-**	**62**	**-**	**-**	**-**	**-**	**62**
Banks, including multilateral development banks (MDBs)	**-**	**-**	**3,372**	**316**	**-**	**18**	**-**	**-**	**3,706**
Securities firms	**-**	**-**	**1,001**	**-**	**-**	**-**	**-**	**-**	**1,001**
Corporations	**-**	**-**	**243**	**-**	**-**	**3,079**	**-**	**-**	**3,322**
Regulatory retail portfolios	**-**	**-**	**-**	**-**	**-**	**24**	**-**	**-**	**24**
Other assets	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
Total	**1,275**	**-**	**4,616**	**378**	**-**	**3,132**	**-**	**-**	**9,401**

	A	B	C	D	E	F	G	H	I
	December 31 2017								
Regulatory portfolio / risk weight	0%	10%	20%	50%	75%	100%	150%	Other	Total credit exposure
	In NIS millions								
Sovereignties	1,252	-	-	-	-	-	-	-	1,252
Public sector entities (PSEs) other than a central government	-	-	-	115	-	-	-	-	115
Banks, including multilateral development banks (MDBs)	-	-	5,065	414	-	36	-	-	5,515
Securities firms	-	-	723	-	-	-	-	-	723
Corporations	-	-	29	118	-	1,549	-	-	1,696
Regulatory retail portfolios	-	-	-	-	-	37	-	-	37
Other assets	-	-	-	-	-	-	-	-	-
Total	1,252	-	5,817	647	-	1,622	-	-	9,338

(a) The disclosed balances refer to the credit exposures used in calculating the capital requirement, after applying credit risk mitigation techniques. The exposures do not include exposures to central counterparties (CCPs) reported in Table CCR8 below.

Composition of Collateral for Counterparty Credit Risk (CCR)[(a)] Exposure (CCR5)

	A	B	C	D	E	F
	December 31 2018					
	Collateral for derivatives transactions				Collateral for securities financing transactions (SFTs)	
	Fair value of received collateral		Fair value of posted collateral		Fair value of received collateral	Fair value of posted collateral
	Encum-bered	Unen-cumbered	Encum-bered	Unen-cumbered		
	In NIS millions					
Cash - local currency	**-**	**101**	**-**	**38**	**310**	**999**
Cash - other currencies	**-**	**9,209**	**-**	**7,073**	**231**	**258**
Local sovereign debt	**-**	**2,380**	**674**	**-**	**1,049**	**326**
Other sovereign debt	**-**	**253**	**-**	**1,880**	**-**	**-**
Government agency debt	**-**	**-**	**-**	**-**	**-**	**-**
Corporate bonds	**-**	**-**	**-**	**-**	**-**	**-**
Shares	**-**	**-**	**-**	**-**	**270**	**242**
Other collateral	**-**	**-**	**-**	**-**	**-**	**-**
Total	**-**	**11,942**	**674**	**8,991**	**1,860**	**1,825**

	A	B	C	D	E	F
	December 31 2017					
	Collateral for derivatives transactions				Collateral for securities financing transactions (SFTs)	
	Fair value of received collateral		Fair value of posted collateral		Fair value of received collateral	Fair value of posted collateral
	Encum-bered	Unen-cumbered	Encum-bered	Unen-cumbered		
	In NIS millions					
Cash - local currency	-	832	-	37	508	1,079
Cash - other currencies	-	4,961	-	3,548	50	81
Local sovereign debt	-	764	700	-	1,133	534
Other sovereign debt	-	197	-	2,015	-	-
Government agency debt	-	-	-	-	-	-
Corporate bonds	-	-	-	-	-	-
Shares	-	13	-	-	85	52
Other collateral	-	-	-	-	-	-
Total	-	6,767	700	5,600	1,776	1,746

(a) The amounts relate to collateral deposited or received in respect of exposures arising from the counterparty credit risk associated with derivatives or securities financing transactions, including transactions settled through a central counterparty (CCP).

Credit derivatives exposures (CCR6)

As of December 31 2018 and December 31 2017, the Bank has no credit derivative transactions that were bought or sold.

Exposures to central counterparties (CCR8)

		A	B	A	B
		December 31			
			2018		2017
		EAD after CRM	RWA	EAD after CRM	RWA
		In NIS millions			
1	**Exposures to Qualified Central Counterparties (QCCP)**	**1,273**	**130**	1,598	193
2	Exposures to transactions with QCCP (excluding primary collateral and transfers to default fund), of which:	**1,273**	**130**	1,598	193
4	Marketable derivative transactions on the stock exchange	**1,273**	**130**	1,598	193
9	Funds transferred to a default fund	**87**	**-**[(a)]	101	-[(a)]

(a) The risk-weighted assets for the default fund were included in the series of exposures to the QCCP transactions above, in accordance with the formula for calculating the risk-weighted assets for central counterparties in Proper Banking Management Directive No. 203.

Market risk

Part 6 - Market Risk - General

General Information about Market risk

Market Risk (MRA)

Market risk is defined the risk of a loss arising from a change in the value of assets and liabilities due: to changes in price levels in the markets, interest rates, exchange rates, inflation rate and stock prices. 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 equity securities and mutual 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 which includes three lines of defense. For a description of the organizational structure and risk management purviews, please see the section entitled "Additional Information on Risk Exposure and Assessment"

The Corporate Governance Structure for Market Risk Management

In addition to the corporate governance structure of risk management at the Bank, which is described in the above section entitled "Additional Information on Risk Exposure and Assessment", following is additional information regarding 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 transactions' life. The Division manages the Bank's own (nostro) account, operates the Bank's dealing room for trading and brokering in currencies, interest rates, derivatives and securities, and is responsible for financial management, which includes developing financial products and investment products as well as managing the Group's assets and liabilities. Control procedures are implemented in the dealing rooms, which are also monitored on an ongoing basis for market risks, operational risks and embezzlement and fraud risks by the Planning Room of the Division's risk management department. The Capital Markets Division is aided by Leumi's investment arm – Leumi Partners.

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.

Second Line of Defense - Risk Management Division

The Division is responsible for examining the market and liquidity risks management from a comprehensive perspective, by formulating the risk policy and risk boundaries from an overall perspective of the Bank's own (nostro) account and dealing rooms, the Bank's non-financial 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 performing stress scenarios, etc.

Third Line of Defense - the Internal Audit Division

The Internal Audit Division is responsible for conducting independent, objective audits while the challenging controls, processes and automated systems in the banking corporation. Audits are usually performed retroactively on the first and second lines of defense, ensuring implementation of the instructions of management and the Board of Directors

The Group's Risk Appetite

The Group's risk appetite is reflected in the level of market risk exposure that the Group is prepared to undertake in order to achieve its business goals and the required return for its shareholders. Alternatively, risk appetite has been defined as the effect of an adverse event that the Group is willing to bear. The risk appetite includes qualitative statements relating to the level of risk that is acceptable to the Board of Directors and senior management and quantitative restrictions for losses that the Group is prepared to absorb under scenarios of various severity levels.

Market Risk Management Policy

The Market risk management policy reflects 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, dealing rooms and market exposure across the entire Leumi Group. The policy outline the corporate governance, division of organizational responsibility and escalation mechanisms. The risk appetite is reflected in set restrictions.

It should be noted that there were no material changes in the Bank's credit policy in 2018.

The market risks are routinely managed at the Group level. The foreign subsidiaries determine their market risk management policies in line with the Group’s policies and its approved risk frameworks, as well as according to the local regulation and business environment in which they operate. 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 by two risk centers – the banking book and the trading book. The definition of the trading book is derived from the Basel rules and includes the Bank's marketable securities portfolio and derivative transactions as part of its trading activity, which are not necessarily for hedging purposes. The trading activities are performed by dedicated units. The banking book includes those trading transactions which are not included in the trading book.

To monitor and control the implementation of the market risk management policy, the Board of Directors receives a report on key market risk exposures against assigned limitations at least once every quarter, underscoring the key risks by business line, product and risk center, and reporting exceptional events.

The Banking Book

The market risks embodied in the banking book arise from the Bank’s core activities (primarily credit granting, deposit taking and securities investments in the available-for-sale portfolio and the held-to-maturity portfolio). The key market risks in the portfolio are interest rate risk, marketable credit spread risk and underlying exposures. The main tools for managing the exposures in the banking book are: the price policy; the management of the Bank’s own (nostro) available-for-sale portfolio and held-to-maturity portfolio; the issue of debt instruments; and hedging through 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.

As part of the exposure management tools, the Bank hedges the exposures to foreign currency and interest rate risks by derivative financial instruments, which help maintain the desired position within the prescribed risk appetite and limits. In addition, activities in derivatives are performed other than for hedging purposes.

The Bank's policy on transactions in derivative financial instruments with entities required to meet capital adequacy requirements is a mechanism for the deposit of mutual collateral - Credit Support Annex (CSA) agreements. For more information, please see Part 5A - "Counterparty Credit Risk".

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 risk, credit margins, equity securities and mutual funds.

The Investment Policy

Leumi's own account (nostro) activity constitutes a principal tool for managing the assets and liabilities, assets and liabilities by linkage base, routing capital and generating profits. It is managed by taking a comprehensive perspective, including addressing all risks and opportunities, including the own account portfolios, the non-financial holdings and assets and the liabilities of the pension portfolio. The investment policy is also subject to risk appetite limits set by the Board of Directors and capital charge required under the Basel Rules. The main 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.

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

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

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

Trading Book

The market risks embodied in the trading book arise from the Bank's activity as a market maker, broker and positions manager for its own (nostro) account. Pursuant to the Bank's policy, instruments are classified into the trading book, which aims to generate profits from trading, while responding quickly to changes in the markets.

Leumi trades in a very broad range of derivatives with various underlying assets: currencies, interest rates, indices, 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 book, proactive actions are taken such as proactive exposures to interest, foreign currencies and tradable credit risks.
Almost daily, market risks in the trading book are identified, monitored, and controlled against the limits - by the Capital Markets Division.

Classification of securities into the trading book is performed for positions which are commercial in nature. The trading activities are subject to limitations, such as portfolio size restriction, interest exposure limit, foreign exchange exposure and more. The classification is based on policies and work procedures, pursuant to the regulatory requirements.

Exposure to Market Risks Arising from Employee Pension Liabilities

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 within the banking book and partly in an independent and separate manner against “plan assets”, with the purpose of achieving long term returns to service the obligation’s value. The long-duration actuarial obligation to employees is significantly affected by changes in the discount interest. The discount rate, which is used for calculating the actuarial liabilities for employee benefits, according to the Bank of Israel’s directives, is based on the Government of Israel's bond yield curve plus the fixed spread curve of internally AA-graded corporate bonds which match the durations of the liabilities for employee benefits.

In 2016, the Bank received an individual approval from the Bank of Israel, under which, for the purpose of capital adequacy measurement, the actuarial liability for employees may be discounted according to an eight-quarter moving average of market yields, which are affected, as aforesaid, by the Government of Israel’s bond curve and by the U.S. AA corporate bond spread. The approval significantly moderated the volatility of the regulatory capital resulting from changes in the discount interest rate. The approval is in effect until December 31 2020, inclusive.

Against part of the actuarial liability, there is an investment in the "plan assets”, that is intended to service the obligation, through investment in diverse and diversified assets such as stocks and debt assets. The investment is subject to regulatory restrictions and limits set by the funds managing the plan assets.

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 metrics 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 raise a red flag in case of an extreme market scenarios.

When estimating a risk using VaR, adjustments are made according to the nature of a portfolio’s activity and composition - for the trading book, it is calculated with a holding horizon of ten business days, and in the banking book - with a holding horizon of one month, both at a significance level of 99 percent. In addition, a back test 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 books. 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 Book VaR at the Group level, According to a Historical Simulation:

	Trading book VaR	
	December 31	
	2018	2017
	In NIS millions	
Actual	**21**	8

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.

Following are the main stress scenarios applied:

- Macroeconomic scenarios developed on a historical basis as well as scenarios of the Bank of Israel based on a crisis in Europe and a crisis in the Israeli real estate market.
- Scenarios based on parallel and non-parallel changes as well as scenarios based on historical changes in accordance with Proper Conduct of Banking Business No. 333.

The Scope and Nature of Risk Measurement Systems

There are two main market risk management systems.
One system interfaces daily with all of the Bank's infrastructure systems and collects the Bank's stock of transactions. The system schedules the cash flows of all transactions, both by the expected payment date and by the interest rate change date. Based on the data, market risk and liquidity exposures are calculated subject to risk management assumptions.
Additional systems are used to manage and operate the nostro portfolio and dealing rooms positions, including pricing, trading and managing exposures.

Market Risk Under Standardized Approach

Market Risk Under Standardized Approach (MR1)

The following table outlines the risk-weighted assets in respect of exposure to market risks under the standardized approach, which covers only some of market risk exposures.

		A	A
		December 31	
		2018	2017
		Risk-weighted assets (RWAs)	
		In NIS millions	
	Direct products		
1	Interest rate risk (collective and specific)	**3,397**	3,373
2	Equity risk (general and specific)	**18**	148
3	Foreign exchange rate risk	**1,046**	687
	Options		
7	The scenario approach	**1,740**	156
8	**Securitization**	**94**	100
9	Total	**6,295**	4,464

Part 6A - Interest Rate Risk in the Banking Book (IRRBB) and Trading Book

IRRBB Risk Management Objective and Policies

Interest rate risk is the risk of profit or capital due to interest rate fluctuations and arises from several sources, such as: Repricing risk (timing differences in repayment periods and repricing of assets, liabilities and off-balance sheet positions); yield curve risk (unexpected yield curve fluctuations); basis risk (imperfect correlation to changes in interest rates in different financial markets or different instruments similar to the repricing characteristics); and optional risk (change in timing or scope of cash flow from a financial instrument due to changes in market interest rates).

The Bank manages the sensitivity of the Bank's economic value to possible interest rate changes and examines the effect of changes in interest rate curves on economic value, under various interest rate assumptions, including scenarios of extreme interest rate changes based on historical scenarios and hypothetical simulations. The Bank also uses a model to estimate the change in projected financing income, as a result of interest rate changes and future spread and sensitivity of the regulatory capital, which includes the effects on the capital and the capital reserve of sudden interest rates change. These metrics have limitations at different hierarchy levels.

As a rule, interest sensitivity is measured at least once a month, with more frequent measurements being made for exposure management purposes.

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 following tools are employed for managing and hedging the exposures of the banking book: the price policy; management of the bonds portfolio; issuing debt instruments; hedging through derivatives, etc. As part of its assets and liabilities management system, the Bank financially hedges some of the interest rate risk through derivatives. This activity cannot be characterized as hedging under the hedge accounting rules. Therefore, changes in the fair value of the derivatives are recognized in the income statement as incurred. Exposures management also relies, inter alia, on projections and assumptions about expected developments in the financial and capital markets in Israel and worldwide.

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 assets and liabilities structure.

Key Behavioral Models Applied to Risk Management

The interest rate risk management models applied reflect customers' behavioral assumptions about the repayment dates of assets and liabilities, the main ones being:

- A model that assumes there is a hard core of (stable) current accounts that is insensitive to the interest rate, treating them as a long-term liability, which is spread over time and is based, inter alia, on a historical examination of the current account balances. In addition, the Bank assumes that there is an additional amount of current account balances that, in case of an interest rate hike, will be spread over a significantly shorter period of time than the stable current accounts.
- A model for forecasting early repayment of mortgages that examines, inter alia, the economic viability of early repayment as a function of the interest rate, customer preferences and behavioral assumptions based on past data.
- A model for early withdrawal from savings plans and deposits at exit points which estimates the expected rate of withdrawals according to various criteria based on historical data.

- To predict early repayments of mortgage products in the nostro portfolio, the Bank uses an external system to examine, among other things, the duration of the current mortgage portfolio, and the effects of interest rate changes on the portfolio's duration and asset value.

The independently developed models undergo regular validation and calibration, and vendor models are challenged using accepted methodologies.

Quantitative Disclosure Regarding Behavioral Models

The average repricing period for on-demand deposits is 1.01 years.
The longest repricing period for on-demand deposits is 10 years.

Following are the Main Restrictions on Exposure to Market Risks as at December 31 2018:

Restriction	In NIS millions
Sensitivity of the economic value to parallel interest rate changes of 1%	
The banking book in NIS	**1,000**
The banking book in foreign currency	**400**
The trading book in NIS	**300**
The trading book in foreign currency	**200**
VaR red flags	
Banking book	**700**
Trading book	**250**

During 2018, the Group complied with all interest exposure restrictions set by the Board of Directors.

Quantitative Information on Interest Rate Risk in the Banking Book (IRRBB) and Trading Book

Adjusted Net Fair Value of the Financial Instruments of the Bank and its Subsidiaries

	December 31 2018				
	NIS		Foreign currency		
	Non-linked	CPI-linked	USD	Other	Total
	In NIS millions				
Financial assets[b]	**295,407**	**44,887**	**47,607**	**33,415**	**421,316**
Other amounts receivable in respect of derivative and compound off-balance-sheet financial instruments	**245,483**	**8,204**	**214,324**	**133,049**	**601,060**
Financial liabilities[b]	**246,928**	**31,696**	**80,622**	**44,403**	**403,649**
Other amounts payable in respect of derivative and complex off-balance-sheet financial instruments	**269,051**	**12,692**	**185,399**	**123,044**	**590,186**
Net fair value of financial instruments	**24,911**	**8,703**	**(4,090)**	**(983)**	**28,541**
Effect of the liabilities for employee benefits	**-**	**(15,511)**	**(183)**	**(173)**	**(15,867)**
Effect of the spread of demand deposits over periods	**1,702**	**-**	**2,297**	**32**	**4,031**
Adjusted[a] net fair value of the financial instruments of the Bank and its subsidiaries	**26,613**	**(6,808)**	**(1,976)**	**(1,124)**	**16,705**
Of which: Banking book	**20,727**	**(7,264)**	**(2,195)**	**(1,033)**	**10,235**

	December 31 2017				
	NIS		Foreign currency		
	Non-linked	CPI-linked	USD	Other	Total
	In NIS millions				
Financial assets[b]	293,416	45,077	47,023	29,202	414,718
Other amounts receivable in respect of derivative and compound off-balance-sheet financial instruments	219,364	7,058	187,695	102,723	516,840
Financial liabilities[b]	247,997	32,634	74,611	39,138	394,380
Other amounts payable in respect of derivative and complex off-balance-sheet financial instruments	238,904	12,295	162,084	94,164	507,447
Net fair value of financial instruments	25,879	7,206	(1,977)	(1,377)	29,731
Effect of the liabilities for employee benefits	-	(17,619)	(196)	(180)	(17,995)
Effect of the spread of demand deposits over periods	883	-	663	774	2,320
Adjusted[a] net fair value of the financial instruments of the Bank and its subsidiaries	26,762	(10,413)	(1,510)	(783)	14,056
Of which: Banking book	22,877	(11,218)	(1,608)	(778)	9,273

(a) Net fair value of financial instruments, excluding non-monetary items and after the effect of employee benefit liabilities and spread of on-demand deposits over the periods.
For more information regarding the assumptions used to calculate the fair value of the financial instruments, please see Note 34A to the Financial Statements.

(b) Excluding total balance sheet derivatives, the fair value of off-balance-sheet instruments and of fair value of compound financial instruments.

Effect of Scenarios of Interest Rate Changes on the Net Adjusted Fair Value[(a)] of the Bank and its Subsidiaries

	December 31 2018				
	NIS		Foreign currency		
	Non-linked	CPI-linked	USD	Other	Total[(d)]
	In NIS millions				
Concurrent changes					
Concurrent increase of 1%	**(101)**	**1,120**	**151**	**84**	**1,254**
Of which: Banking book	**(42)**	**1,124**	**136**	**76**	**1,294**
Concurrent decrease of 1%	**58**	**(1,456)**	**(299)**	**(90)**	**(1,787)**
Of which: Banking book	**(2)**	**(1,459)**	**(286)**	**(82)**	**(1,829)**
Non-concurrent changes					
Steepening[(b)]	**234**	**1,209**	**42**	**24**	**1,509**
Of which: Banking book	**268**	**1,206**	**41**	**23**	**1,538**
Flattening[(c)]	**(265)**	**(1,045)**	**(8)**	**(6)**	**(1,324)**
Of which: Banking book	**(287)**	**(1,042)**	**(11)**	**(7)**	**(1,347)**
Short-term interest rate hike	**(264)**	**(399)**	**100**	**30**	**(533)**
Of which: Banking book	**(257)**	**(395)**	**91**	**26**	**(535)**
Short-term interest rate decrease	**291**	**432**	**(92)**	**(31)**	**600**
Of which: Banking book	**286**	**428**	**(84)**	**(27)**	**603**

	December 31 2017				
	NIS		Foreign currency		
	Non-linked	CPI-linked	USD	Other	Total[(d)]
	In NIS millions				
Concurrent changes					
Concurrent increase of 1%	146	1,650	165	99	2,060
Of which: Banking book	146	1,633	189	57	2,025
Concurrent decrease of 1%	(120)	(2,058)	(150)	(108)	(2,436)
Of which: Banking book	(104)	(2,040)	(184)	(62)	(2,390)
Non-concurrent changes					
Steepening[(b)]	391	1,423	(105)	46	1,755
Of which: Banking book	422	1,417	(121)	34	1,752
Flattening[(c)]	(347)	(1,149)	145	(60)	(1,411)
Of which: Banking book	(374)	(1,147)	157	(58)	(1,422)
Short-term interest rate hike	(245)	(255)	152	(69)	(417)
Of which: Banking book	(268)	(260)	182	(85)	(431)
Short-term interest rate decrease	279	288	(149)	72	490
Of which: Banking book	315	294	(183)	88	514

(a) Net fair value of financial instruments, excluding non-monetary items and after the effect of employee benefit liabilities and spread of on-demand deposits over the periods.
(b) Steepening - short term interest rate decrease and long-term interest rate increase.
(c) Flattening - short term interest rate hike and long-term interest rate decrease.
(d) After netting effects

Effect of Scenarios of Interest Rate Changes on the Interest Income and Noninterest Income, Net[a]

	For the year ended December 31					
	2018			2017		
	Interest income	Noninterest finance income	Total[b]	Interest income	Noninterest finance income	Total[b]
	In NIS millions					
Concurrent changes						
Concurrent increase of 1%	**591**	**226**	**817**	508	310	818
Of which: Banking book	**591**	**281**	**872**	508	315	823
Concurrent decrease of 1%	**(591)**	**(223)**	**(814)**	(508)	(244)	(752)
Of which: Banking book	**(591)**	**(281)**	**(872)**	(508)	(315)	(823)

(a) The exposure to a 1 percent 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 percent, and there is a low probability that the interest on deposits will fall below 0 percent, the above exposure calculation should be considered a measure in line with the accepted standards.

(b) After netting effects

Additional Information about Interest Rate Risk

Total Exposure of the Bank and its Subsidiaries to Interest Rate Changes

	December 31 2018				
	Demand of up to one month	More than one month to three months	More than three months to one year	More than one year and up to three years	More than three years and up to five years
	In NIS millions				
Financial assets[(a)]	**268,642**	**26,487**	**38,643**	**35,759**	**22,249**
Other receivables[(b)]	**124,449**	**184,864**	**143,821**	**75,050**	**33,715**
Financial liabilities[(a)]	**231,892**	**19,289**	**48,804**	**65,210**	**13,729**
Other payables[(b)]	**121,220**	**168,961**	**156,259**	**72,130**	**32,945**
Exposure to interest rate changes	**39,979**	**23,101**	**(22,599)**	**(26,531)**	**9,290**
More information on exposure to interest rate changes					
a. By nature of activity[(e)]					
Exposure of the banking book	**38,587**	**9,972**	**(13,546)**	**(25,767)**	**7,107**
Exposure of the trading book	**1,392**	**13,129**	**(9,053)**	**(764)**	**2,183**
b. By linkages bases[(e)]					
Unlinked NIS	**37,825**	**11,687**	**(6,428)**	**(24,045)**	**5,107**
CPI-linked NIS	**422**	**704**	**1,876**	**(6,062)**	**2,192**
Foreign currency (including linked to foreign currency)	**1,732**	**10,710**	**(18,047)**	**3,576**	**1,991**
c. Effects of exposure to interest rate changes[(d)]					
Effect of the liabilities for employee benefits	**62**	**123**	**554**	**1,304**	**1,362**
Effect of the spread of demand deposits over periods	**(66,643)**	**10**	**15,947**	**27,975**	**5,401**
Effect of early repayment of housing loans	**326**	**303**	**1,108**	**1,521**	**(120)**
Effect of backed assets	**38**	**98**	**652**	**942**	**400**

(a) Excluding total balance sheet derivatives, the fair value of off-balance-sheet instruments and of fair value of compound financial instruments, after the effect of spread of demand deposits over periods.

(b) Receivables and payables in respect of derivative, compound and off-balance-sheet financial instruments after the effect of liabilities for employee benefits. Compound financial instruments were classified according to each instrument's effective average life as exposure to their interest rates cannot be reflected by their classification into repayment periods of cash flows or nearest interest rate change date.

(c) Weighted average by fair value of the average duration.

(d) The effects on the duration and internal rate of return (IRR) relate to the effects of each of the models on the total balance in the item.

(e) The reported duration is the difference between the duration of the total assets and the duration of the total liabilities.

							December 31 2017		
More than five years and up to ten years	More than ten years and up to twenty years	Over twenty years	Without loan term	Total fair value	Internal rate of return	Average effective life(c)	Total fair value	Internal rate of return	Average effective life(c)
					In %	In years		In %	In years
19,747	**6,266**	**2,759**	**764**	**421,316**	**2.65%**	**1.16**	414,718	2.57%	1.02
37,355	**1,347**	**458**	**1**	**601,060**	**-**	**1.09**	516,840	-	1.29
19,462	**280**	**944**	**8**	**399,618**	**2.02%**	**0.96**	392,060	2.11%	0.95
44,329	**5,761**	**4,448**	**-**	**606,053**	**-**	**1.48**	525,442	-	1.78
(6,689)	**1,572**	**(2,175)**	**757**	**16,705**	**-**	**-**	14,056	-	-
(6,219)	**1,602**	**(2,258)**	**757**	**10,235**	**-**	**(0.30)**	9,273	-	0.43
(470)	**(30)**	**83**	**-**	**6,470**	**-**	**0.01**	4,783	-	(0.01)
(911)	**2,175**	**645**	**558**	**26,613**	**-**	**(0.02)**	26,740	-	(0.11)
(995)	**(2,120)**	**(2,834)**	**9**	**(6,808)**	**-**	**(1.62)**	(10,414)	-	(1.66)
(4,783)	**1,517**	**14**	**190**	**(3,100)**	**-**	**(0.04)**	(2,270)	-	(0.01)
3,385	**5,191**	**3,886**	**-**	**15,867**	**2.74%**	**14.52**	17,995	2.06%	14.24
13,279	**-**	**-**	**-**	**(4,031)**	**1.82%**	**1.01**	(2,320)	0.93%	0.98
(175)	**(1,798)**	**(732)**	**-**	**433**	**(0.17%)**	**(0.48)**	714	(0.20%)	(0.42)
(81)	**(956)**	**(738)**	**-**	**355**	**(0.27%)**	**(2.87)**	-	-	-

Additional Disclosure Regarding Compound Financial Instruments

Fair Value, Effective Average Life and Effect of the Interest Rate Changes and of Hypothetical Changes in the Interest Rates on the Fair Value of Compound Financial Instruments of the Bank's and its Consolidated Companies.

	December 31 2018					
			Fair value assuming changes in interest rates			
		Average effective	Increase of:		Decrease of:	
	Fair value	life	2%	1%	2%	1%
	In NIS millions	In years	In NIS millions			
Foreign currency segment						
Compound financial assets:						
Backed assets	**11,287**	**3.03**	**10,538**	**10,936**	**11,741**	**11,562**
Total compound financial assets	**11,287**	**3.03**	**10,538**	**10,936**	**11,741**	**11,562**
Total change in the fair value of compound financial instruments, net as a result of interest rate changes			**10,538**	**10,936**	**11,741**	**11,562**

For more information regarding the assumptions used to calculate the fair value of the financial instruments, please see Note 34A to the Financial Statements.

Disclosure of Interest Exposures According to the Economic Valuation Method

Summary of Exposures to Unexpected Interest Rates Changes at the Group level (Before the Tax Effect) [(a)]

	The potential change in economic value as a result of the scenario					
	December 31 2018			December 31 2017		
	Increase of 1%	Decrease of 1%	Increase of 0.1%	Increase of 1%	Decrease of 1%	Increase of 0.1%
Scenario	In NIS millions					
in NIS						
Banking book	**(765)**	**707**	**(79)**	(411)	306	(41)
Trading book	**(62)**	**63**	**(7)**	(38)	25	(3)
In foreign currency						
Banking book	**62**	**(221)**	**6**	175	(249)	22
Trading book	**6**	**(3)**	**1**	32	47	2

	The potential change in the annual net income from a 1% interest rate increase[(b)]			
	December 31 2018		December 31 2017	
	in NIS	Foreign currency	in NIS	Foreign currency
Total	**418**	**391**	417	391

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

(b) A decrease in interest rate is expected for result in a similar loss amount.

The increase in the interest rate exposure in foreign currency in the banking book is mainly due to purchases for the held-to-maturity portfolio and credit provision. In foreign currency, the increase is due to increased exposure of the nostro portfolios.

Capital Exposure to an Immediate Increase or Decrease in Interest Rates (Before Tax)

	Exposure in NIS			Exposure in foreign currency		
	December 31 2018					
	Increase of 1%	Decrease of 1%	Increase of 0.1%	Increase of 1%	Decrease of 1%	Increase of 0.1%
	In NIS millions					
Capital exposure to an immediate increase/decrease in interest rates[(a)]	**1,336**	**(1,685)**	**147**	**(519)**	**473**	**(52)**

	Exposure in NIS			Exposure in foreign currency		
	December 31 2017					
	Increase of 1%	Decrease of 1%	Increase of 0.1%	Increase of 1%	Decrease of 1%	Increase of 0.1%
	In NIS millions					
Capital exposure to an immediate increase/decrease in interest rates[(a)]	1,615	(2,083)	180	(349)	352	(34)

(a) 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 2018 - to be a NIS 122 million decrease in the value of the assets (on December 31 2017 - NIS 134 million) under a scenario of a 1 percent interest rate increase. Neither does the measurement include the effects of the transitional provisions of the Employee Benefits Standard, on which the capital adequacy ratio calculation is based.

Part 6B - Equity Risk

Risk of investment in equity securities and mutual funds, caused by impairment of the investment in equity securities and mutual funds or by a decline in profits or dividends paid to the Group. This exposure is managed in accordance with the nostro portfolios' investment policy, which stipulates limitations on both the total investment amount and per-company amount.

According to the investment policy, the Bank's investment activities include investing in marketable mutual funds, indices and ETFs, rather than in specific shares, while maintaining a high level of diversification. In addition, investing activities is carried out by subsidiary Leumi Partners, pursuant to the Group's investment policy.

The fair value of the marketable equity securities is determined according to the market value and the fair value of the non-marketable equity securities is measured at cost (less a provision for impairment of a non-temporary nature).

Investment in Equity Securities and Mutual Funds and the Banking Book

	December 31			
	2018		2017	
	Fair value	Capital requirements[(a)]	Fair value	Capital requirements[(a)]
	In NIS millions			
Non-tradable equity securities in the available-for-sale portfolio	**1,079**	**148**	991	136
Tradable equity securities and mutual funds in the available-for-sale portfolio	**2,477**	**341**	1,936	266
Total	**3,556**	**489**	2,927	402

(a) The capital requirements were calculated in accordance with the minimum total capital required by the Banking Supervision Department at a rate of 13.75 percent as at December 31 2018 and 13.75 percent as at December 31 2017.

Part 7 - Liquidity Risk

Liquidity risk is the risk arising due to uncertainty regarding the possibility of raising resources 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 Conduct of Banking Business 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 stock 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 a "stock 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 amount 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 percent.

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 liquidity risk management policy

Leumi maintains a proper liquidity level by investing its own portfolio in high-quality, 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 bonds.

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 restrictions on the liquidity ratio under Directive No. 221 were set at several levels of management, primarily by the Board of Directors. These restrictions constitute yet another reserve for meeting the liquidity scenarios.

Liquidity Coverage Ratio (LCR) - Main Disclosures Table (LIQ1)

		For the three months ended December 31			
		2018		2017	
		(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			
1	Total high-quality liquid assets (HQLA)		**112,238**		113,298
	Cash outflows				
2	Retail deposits from individuals and small businesses	**177,557**	**12,532**	174,315	12,227
3	Of which: Stable deposits	**48,742**	**2,437**	45,061	2,253
4	Less stable deposits	**73,288**	**8,429**	69,571	8,184
4A	Deposits for a period exceeding 30 days	**55,527**	**1,666**	59,683	1,790
5	Unsecured wholesale financing	**146,735**	**96,374**	141,073	93,293
7	Of which: Non-operational deposits (all counterparties)	**146,686**	**96,325**	140,776	92,996
8	Unsecured debts	**49**	**49**	297	297
10	Additional liquidity requirements	**67,949**	**8,017**	70,162	9,516
11	Of which: Outflows in respect of exposure to derivatives and other security requirements	**2,964**	**2,964**	4,091	4,091
13	Credit lines & liquidity	**64,985**	**5,053**	66,071	5,425
14	Other contractual financing commitments	**5,935**	**5,935**	6,049	6,049
15	Other contingent financing commitments	**40,603**	**1,293**	41,055	1,330
16	**Total cash outflows**		**124,151**		122,415
	Cash inflows				
17	Secured loans (e.g., reverse repurchase transactions)	**1,161**	**-**	1,346	-
18	Cash inflows from regularly repaid exposures	**43,885**	**29,182**	41,119	27,538
19	Other cash inflows	**9,647**	**2,346**	8,817	2,120
20	**Total cash inflows**	**54,693**	**31,528**	51,282	29,658
	Total adjusted value(c)				
21	Total high-quality liquid assets (HQLA)		**112,238**		113,298
22	Total cash outflows, net		**92,623**		92,757
23	Liquidity coverage ratio (in %)		**121%**		122%

(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 76 daily observations during Q4 2018 (79 observations during Q4 2017).

In the past year, the liquidity coverage ratio was higher than the regulatory restrictions. The ratio was mainly affected by an increase in the volume of retail deposits and against a decrease in deposits of ETF customers that were deposited for long periods due to restrictions imposed on these clients under Amendment 28 to the Joint Investment Trust Act (ETFs and market making) and the provision of credit to the public.

Additional Disclosures regarding Liquidity Coverage Ratio (LIQA)

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, reporting on the exposures is presented to the Board of Directors and management at least once each quarter.

The exposure to liquidity risks is regularly managed at the Group level and a Group-level monitoring process is being developed. The subsidiaries establish liquidity risk management policies and manage their liquidity ratio independently, in line with the Group's policy and subject to the local regulatory framework applicable to each company. When managing its liquidity and calculating the LCR, the Bank takes into account possible limitations on transferring liquidity between the Bank and its subsidiaries. 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. Therefore, the Bank does not rely on the lines set as part of the ongoing activity.

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

Composition of High-Quality Liquid Assets by Average Balance Per Quarter

	For the three months ended December 31					
	2018			2017		
	NIS	Foreign currency	NIS and foreign currency	NIS	Foreign currency	NIS and foreign currency
	Total weighted value in NIS millions					
Total Tier 1 assets	**84,157**	**20,987**	**105,144**	86,328	23,562	109,890
Total Tier 2A assets	**-**	**6,879**	**6,879**	-	3,153	3,153
Total Tier 2B assets	**106**	**109**	**215**	45	210	255
Total high-quality liquid assets	**84,263**	**27,975**	**112,238**	86,373	26,925	113,298

Composition of High-Quality Liquid Assets as at the End of the Period

	As at December 31					
	2018			2017		
	NIS	Foreign currency	NIS and foreign currency	NIS	Foreign currency	NIS and foreign currency
	Total weighted value in NIS millions					
Total Tier 1 assets	**86,671**	**18,739**	**105,410**	93,573	24,902	118,475
Total Tier 2A assets	**-**	**7,295**	**7,295**	-	3,007	3,007
Total Tier 2B assets	**112**	**130**	**242**	11	255	266
Total high-quality liquid assets	**86,783**	**26,164**	**112,947**	93,584	28,164	121,748

In accordance with the prescribed risk appetite, the Bank's Board of Directors sets restrictions for managing liquidity risk purposes. The Chief Risk Officer sets additional restrictions for ongoing management of liquidity risk.

Additional Information regarding Liquidity Risk and Financing Risk

Liquidity Risk

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.
Leumi maintains a high level of liquidity, which is among its foundations and relative advantages in the local and global banking domain.The basis for Leumi's financing is deposits by the public and debt instruments - which constitute a stable source of financing. The main basis for Leumi's foreign currency is corporate deposits, financial deposits and individual deposits by Israeli residents and nonresidents.

The amount of deposits by the public - by private individuals and small businesses - with Leumi is stable throughout the year. Following is the development of the average balances:

	Unweighted Value of Retail Deposits - 2018			
Period	Q1	Q2	Q3	Q4
Up to one month	**117,722**	**121,001**	**121,256**	**122,030**
More than one month	**55,975**	**55,251**	**55,538**	**55,527**
Total	**173,697**	**176,252**	**176,794**	**177,557**

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 by retail customers. In addition, the Bank finances its activity through deposits made by commercial and business customers and by issuing bonds. The sources are managed on an ongoing basis, separately for NIS and foreign currencies. About 32.5 percent of the public's deposits are raised in foreign currency and linked to foreign currency. The Bank has a wide range of foreign currency sources from nonresidents, and from local retail, business and financial customers. In the past year there has been an increase in financial deposits and a decrease in retail deposits. The excess deposits on the foreign currency credit are invested in liquid assets and short-term swaps. The sources of the foreign offices are invested in credit and liquid assets, primarily low-risk bonds and short-term swaps.

In the NIS retail deposits, there was an increase throughout the year mainly towards its end, whereas in the financial deposits, a decrease was recorded during the reporting period, which was mainly due to the entry into force of Amendment 28 to the Joint Investment Law. During the reporting period, bonds were issued in the amount of NIS 1.3 billion and CoCo bonds - in the amount of NIS 0.8 billion, net.

The concentration of financing sources is managed and monitored using risk management indicators and models. The Bank follows up on the composition and concentration of sources by several categories: customer size and type, single depositor, the 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 metrics, 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.

Pledged Assets by Balance Sheet Line Item

	December 31 2018			
	Pledged assets associated with			
	Securing deposits	Clearing house and risk reserve activities	CSA agreements	Activities in derivatives
	In NIS millions			
Cash and deposits with banks	**-**	**-**	**2,639**	**4,338**
Securities	**1,925**	**813**	**-**	**1,880**
Loans to the public	**-**	**80**	**96**	**-**

	December 31 2017			
	Pledged assets associated with			
	Securing deposits	Clearing house and risk reserve activities	CSA agreements	Activities in derivatives
	In NIS millions			
Cash and deposits with banks	-	-	495	1,289
Securities	4,178	930	-	2,015
Loans to the public	-	80	1,764	-

Additional Risks

Part 8 - Operational Risk

Operational risk is defined as 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 cyber risks, technological risk, business continuity risk as well as embezzlement and fraud risks.

The risk management approach is consistent with the strategy of the Leumi Group, constitutes a basis for defining the risk tolerance, for the manner in which risk is managed, and for the corporate governance. It also determines the focus and emphases in operational risk management processes, allowing for informed and focused risk management, which prioritizes tasks and resources.

The regulatory capital in respect of operational risk is calculated using the standardized approach in the Banking Supervision Department's capital adequacy measurement provisions.

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

Corporate Governance Structure

In addition to the corporate governance structure of risk management at the Bank, which is described in the above section entitled "Additional Information on Risk Exposure and Assessment", following is additional information regarding operational risk management:

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 Cyber Risk Department in the Risk Management Division is responsible for, and leads, the operational risk management process, while developing recommendations for the risk management policy and risk tolerance, developing methodologies and professional responsibility, instructing and challenging (subject to materiality considerations) of the first line of defense in the risk management process.

Third line of defense - the Internal Audit Division The Internal Audit Division is responsible for conducting independent, objective audits while the challenging controls, processes and automated systems in the banking corporation. Audits are usually performed retroactively on the first and second lines of defense, ensuring implementation of the instructions of management and the Board of Directors

Management and Board of Directors' committees - Each quarter, the committees hold a discussion on the material exposures to operational risks. Each year, 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 framework, 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 statements.

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 and documentation of controls, mitigation plans and failure events.

The Bank manages risks for 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 risks are cross-organizational, the Risk Management Division works to instill an advanced risk management culture, including reporting on incidents and drawing conclusions.

The Main Operational Risk Areas are as Follows:

Information Security and Cyber Risk

Leumi continues to promote the provision of financial services through digital platforms, expanding the use of advanced technologies. As a result, the risk of cyber-attacks is growing, as is Leumi’s exposure to the materialization of cyber risks.

Cyberspace is highly dynamic and characterized by uncertainty in terms of the type, scope and force of the attacks. A materialization of a cyber event may result in monetary damage, theft of sensitive banking information, disruption of activity and operational continuity and even damage to the Bank’s reputation.

Risk management and cyber security are implemented, with significant resources invested. Resources are invested differentially, in accordance with the business strategy and risk tolerance.

As part of its effort to boost its cyber defenses and manage cyber risk, Leumi developed and implements a cyber policy. The policy stresses the prevention of material events and development of tools and capabilities to counteract them, in case they indeed occur. Recently, a new Fusion Center was established to allow for the implementation of cyber and security approach and improve response capabilities and event management in real time.

In 2018, no cybersecurity incidents were discovered which affected Leumi'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 activity. The IT environment is complex, ever-changing and organizations are becoming increasingly dependent on it.

Leumi 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.

In light of the above, and in order to ensure that the systems are up to date, that the business and technological elasticity increases and to improve the system’s stability, Leumi is at the final planning stages of a project to replace its core systems. This significant project will take several years to complete, and will have milestones in line with Leumi’s business lines.

Business Continuity Risk

Leumi manages and implements processes whose purpose is to enable rapid recovery and return to normal in case of emergencies and extreme cases, while minimizing damage to business activities. The processes include the following:

- A business continuity policy that defines corporate governance, principles, and the key processes in case of an emergency.
- Development and implementation of a work framework that includes business continuity plans, business impact analysis, recovery strategies and a drill methodology.
- Preserving the stability of technological infrastructures, providing recovery capabilities including backup and recovery capabilities.

Outsourcing and Supplier Risk

Leumi contracts suppliers and sub-suppliers for various business needs and adopts new products and services developed by external entities. Its dependence on suppliers exposes the Bank to various risks, including business continuity disruption and information leakage. Such risks are managed on an ongoing basis through the procurement, information security, business continuity and cybersecurity workflows.

Proper Conduct of Banking Business Directive No. 359A, "Outsourcing"

The purpose of the Outsourcing Directive is to enable banking corporations to implement strategic objectives, increase availability to customers, continue to streamline processes and boost competition in the banking and payments domains, while prescribing the principles banking corporations are to follow in order to reduce their exposure to potential risks embodied in outsourcing. The Directive will become effective in March 2020. The Bank is preparing to implement the directive.

Proper Conduct of Banking Business No. 363, "Supply Chain Cyber Risk Management"

The aim of the Supply Chain Cyber Risk Management Directive is to establish a banking corporation's responsibility to ensure cybersecurity when working with material suppliers and its duty to manage cybers risks adequately when such outsourcers work on its premises – both on the banking corporation's premises and when using the outsourcers' interfaces with the corporation. The Bank is preparing to implement the directive.

For more information regarding the two directives, please see the section entitled "Laws and Regulations Governing the Banking System" in the financial statements.

Embezzlement and Fraud

The digital workplace environment increases the odds 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.

Risk Arising from Restructuring

For several years, Leumi has aimed to adjust its activity model. In this context, it has made significant changes to its corporate structure, and has altered purviews, work procedures, controls, supporting systems as well as its workforce. Such changes may increase the operational risks in the short term, especially the risk of human error. Leumi attributes great importance to maintaining a robust control environment. As a result, the Bank has developed principles and an up-to-date operational approach with the aim of reducing the number of errors and minimizing the potential damage to the business activity.

Part 9 - Additional Information on Other Risks

Regulatory Risk

Regulatory risk is the risk of legislative and regulatory changes affecting the Group's total income and expenses, capital, areas of activity or the business environment in which it operates.

The Leumi Group operates in a complex and multidisciplinary regulatory environment. Material ongoing changes in diverse regulatory domains require adequate ongoing preparedness of the Bank's activities.

Recently, significant emphasis has been made on provisions designed to encourage new players to enter into traditional banking, removing barriers and restrictions, as well as provisions intended to promote innovation in the financial system, such as: The provisions of the Law for Increasing Competition and Reducing Concentration in the Banking Market in Israel, a new policy for establishing a banking corporation by the Bank of Israel, promoting the adoption and implementation of the Open API standard designed to enable sharing of financial information between customers and third parties, and new advanced payment legislation.
In addition, the consumer regulation trend continues, including legislation aiming to reduce costs for customers. At the same time, emphasis is made on adapting the various financing products to customers' needs, while providing maximum disclosure and stressing transparent and fair conduct.
Additional trends are manifested in handling the transition to e-banking, outsourcing and use of cloud computing in the financial system, as well as privacy protection and cyber defense. These topics are on the agenda both in Israel and globally, and are reflected in the GDPR requirements, which deal with privacy protection as well as specific cybersecurity and outsourcing directives
The abovementioned changes affect and are expected to continue affecting the banking industry in the coming years. The Bank monitors and identifies relevant regulatory provisions and examines its preparedness to the following: Changing market conditions; increased competition and transparency; entry of new players into traditional banking domains; the Bank's costs compared to those of other entities; use of databases and information of the Bank's customers by non-banking entities as well as providing adequate value propositions to the Bank's customers. At the same time, regulation erodes income, leads to increased compliance costs and requires banks to constantly improve their levels of service and innovation.

Compliance Risk

Compliance risk is the risk of a legal or regulatory sanction being imposed, or a material financial loss or a reputational damage incurred, by the banking corporation as a result of failing to comply with the provisions of the law or regulations.

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.

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.

a. Compliance Risk, Prohibition on 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, pursuant to primary legislation, regulations, ordinances, permits and the Bank of Israel's directives, as well as global regulations and standards governing the Bank's activities. The compliance function is responsible for managing the compliance risk derived from compliance directives and related provisions in the following areas: conflicts of interest, fair conduct, prohibition on money laundering and the financing of terrorism, providing advice to customers, privacy protection, taxation aspects relevant to products or services provided to customers, according to the requirements of the Banking Supervision Department. 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 the Board of Directors, management and Chief Compliance Officer, and the three defense lines’ respective areas of responsibility.

A 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 efficiency of enforcement 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/her function, according to the Criteria List, is to be responsible for implementing the enforcement program.

The Group’s Chief Compliance Officer also serves as an 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 sent 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. The Income Tax (Implementation of a Uniform Standard for Reporting and Due Diligence of Information on Financial Accounts) Regulations was approved by the Finance Committee on January 1 2019. The regulations are based on the CRS agreement of which the State of Israel is a signee.

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.

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 paper has been revised periodically over the years, including in 2018.

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 using a uniform format prepared by the Legal Counsel Division. In 2018, the legal risk management processes and controls alongside them were also updated, and the legal stress scenario was challenged and updated.

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 functions and committees within the Legal Counsel Division. Headed by the Chief Legal Counsel - who also serves as Legal Risk Officer - the Division is responsible for reviewing, coordinating and handling 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 functions 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

The Banks has a 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, interpretational and others, relating to a large number of 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 will be 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 types of lawsuits will be brought against the Bank 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 compromising shareholders' and various stakeholders' trust in the Leumi Group, as a result of conduct, action, or omission by the Group, its employees or other involved parties.

Reputational risk refers to the perceptions of the shareholders, stakeholders, the public, influencers and the media, whether they are fact-based or otherwise. Reputational risk is dynamic and changes depending on various topics and populations.

The reputational risk management policy was approved by the Bank's management and Board of Directors with the view that trust is vital to business activity. The policy defines the organizational structure and areas of responsibility supporting the management of reputational risk.

Strategic Risk

Strategic risk is a business risk whose damage is material and affects the business model of the Bank or of one of its business lines. In fact, this type of risk may have an effect on profit that is insignificant in the immediate term, but which may become significant in the mid- to long term. Strategic risks involve threats that may arise from erroneous business decisions, inadequate implementation of decisions, or failure to respond to sectoral, economic, regulatory, consumer, or technological developments.

The main strategic risk stems from the fact that the financial service industry is undergoing significant digitalization changes. The opening of the banking industry to competition and the entry of new players - such as BigTech (Google, Amazon, Facebook and Apple), Fintech companies, insurers and non-banking credit companies - requires the business model to be adjusted. In addition, the Law for Increasing Competition and Reducing Concentration in the Banking Market in Israel (the "Strum Law") includes components which could strategically impact the competitive map in Israel. One of its direct consequences for Bank Leumi is the sale of Leumi Card. Another strategic topic is open banking.

Strategic risk management is led by the Strategy and Regulation Department, with the involvement of the Risk Management Division and Finance Division. These functions are in charge of identifying, mapping, assessing and monitoring this risk for all of the Bank's units and the Board of Directors.

In view of the new trends and significant changes introduced into its operating environment, Leumi adopted two main courses of action, the combination of which is at the core of the Group strategy. On the one hand, the Bank strives to adapt its traditional banking models without compromising the high-quality professional services it provides to all customer types according to their needs, preferences and attitude to the adoption of digital innovation; on the other hand, the Bank develops its "New Banking" model through digital and technological channels. These two courses of action depend on and are combined with the need to streamline the Bank's activity and maximize capital utilization while meeting capital adequacy targets.

A three year plan, the Bank's strategic risk is approved by management and the Board of Directors. The strategic plan is drawn following a comprehensive process of examining trends and changes in the business environment, competitive environment, technological environment and customer preferences, with the aim of identifying and mapping threats and opportunities.

Each year, the Bank conducts a process to identify banking changes and trends which may affect the Israeli Banking market, while examining the need to revise and adjust the previously-set strategic objectives. The process serves as the basis for formulating the annual work plan and defining the main objectives and projects in the business divisions' work plans, while setting metrics for monitoring, managing and following-up on the implementation of the strategic goals.

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 foresee that outcome. As a result, the Bank may incur losses from lawsuits, 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.

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. Lately, some risks have risen from possible international trade developments, especially the trade relations between the US and China. If the situation escalates to an ongoing “trade war”, it may have an adverse effect on global growth. As a result, the Israeli economy may be indirectly affected as well.

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.

Part 10 - Remuneration

Qualitative Disclosure in Table Format (REMA)

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

Qualitative disclosure

a. Information about the Functions Supervising Remuneration

Name, composition and purview of the main function regulating 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 terms and the underlying principles of other employees' terms of employment.
Details of external consultants the Bank wishes to engage 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 is based on 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, and includes recommended guidelines and principles for the subsidiaries. The remuneration policies for the Bank's officeholders and key employees apply from October 2016 to the end of 2019.
A description of the types of employees defined as officeholders and other key employees.	The Bank's officeholder group comprises the Chairman of the Board and other members of the Board, the President & CEO and other members of management (including the Chief Internal Auditor) as well as two officeholders who are not members of management. The "other key employees" group (who are not officeholders) was determined in line with the definition of the term in Proper Conduct of Banking Business Directive No. 301A.

[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, in accordance with Section 118A(D) to the Companies Law.

b. Information on Planning and Structure of the Remuneration Processes

Review of the main characteristics and objectives of the remuneration policy.	The remuneration policy is based, inter alia, on the provisions of the Companies Law regarding setting the remuneration policy, 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 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 (including salaries and related benefits), 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, in certain cases - deferring the payment of part of the variable bonus, pursuant and subject to the directives of the Banking Supervision Department.
Review of changes made to the Bank's remuneration policy throughout the reporting year, the reasons for the changes and their effect on the remuneration.	In 2018, no changes were made to the remuneration policy applicable to the Bank's officeholders. In May 2018, the remuneration policy for key employees (who are not officeholders) was updated. Under the update , these employees are now eligible for special variable bonuses for success and outstanding excellence. In addition, the remuneration policy for all bank employees was updated in 2018. Under the update, an option was added to grant employees with unique expertise a retention bonus. The updates to the remuneration policy for the key employees (who are not officeholders) and the remuneration policy for all Bank employees are intended to allow greater flexibility in granting appropriate incentives to the relevant employees for the purpose of promoting the Bank's objectives. The updates are not expected to have a material effect on the total annual expense for employees' remuneration at the Bank.
Discussion of the manner in which the Bank ensures that employees who handle risks and compliance are remunerated independently of the businesses they oversee.	The variable annual remuneration structure under the 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, pursuant to the Remuneration Limitation Law, the maximum annual variable bonus is 6 monthly salaries per year (excluding special bonuses), 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

Overview of the main risks, their measurement and the means by which the metrics affect the compensation.	The remuneration policy is aimed at preventing the Bank from undertaking short-term risks and prescribes mechanisms to ensure that the various risks related to its activity are taken into account in determining the variable remuneration amount of the key employees. Thus, for example, the measuring of performance in respect of the measurable variable bonus component - which is based, inter alia, on the Bank's return on capital - is calculated according to the Bank's weighted return on equity over a period of 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. The qualitative personal bonus is based, inter alia, on: compliance with the laws and regulations; compliance with the Bank's policy and 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, etc. In addition, the Board of Directors is authorized to reduce, in certain cases, the measurable variable bonus for officeholders; and the CEO & President is authorized to reduce, in certain cases, the variable bonus to the key employees. The remuneration policy also establishes mechanisms aimed at creating incentives to ensure that the variable bonus 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 clawback 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.

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 metrics - both for the upper level of the business lines and for personal performance.	• The main performance metrics 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; proactively promoting and leading projects; complying with laws and regulations and with the Bank's procedures; not deviating from the Board of Directors' policy; meeting the Bank's risk management policy and risk appetite; 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 metrics are weak including the criteria for determining when the Bank's 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 under the directives of the Banking Supervision Department during the bonus year. In addition, a substantial part of the annual measurable bonus is conditional on the Bank's reaching a minimum of a 6 percent weighted return on equity during the bonus year (calculated over three years, as mentioned above). Another part is conditioned upon reaching a return gap greater than (-1.5 percent) between the annual return on the Bank's share and the annual return on the TA Banks Index, excluding the Bank's share. If the variable remuneration is higher than 40 percent of the annual fixed bonus, a uniform mechanism of deferral whereby half (50 percent) of the amount of the variable bonus 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 stock-based instruments. A deferred bonus will be granted only if, at the designated payment date, the Bank meets its required capital adequacy targets. If not, the payment will be deferred until the said ratio 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 his/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 clawback arrangement	In addition to the aforesaid, a key employee must return to the Bank any amounts paid to him/her 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 (as determined by the Audit 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.	Pursuant to Directive 301A, the variable remuneration in a given year for each of the Bank's key employee shall not exceed 100 percent of the fixed remuneration of that key employee during that year. It should be noted that, pursuant to the remuneration policy, the annual variable salary for officeholders is limited to a maximum of 7 monthly salaries, and the annual variable bonus for key employees who are not officeholders is limited to 6 monthly salaries, excluding special bonuses. In addition, according to the remuneration policy for all other Bank employees, the variable remuneration in a given year for each of the Bank's key employees shall not exceed 85 percent of the fixed remuneration of that employee during that year.
In exceptional cases, where the Bank has determined that the maximum variable remuneration may exceed 100 percent of the fixed remuneration - details of the ratios set, the reasons thereto, the affected employees, their position and the effect on the Bank.	As aforesaid, the maximum variable remuneration may not exceed 100 percent of the fixed remuneration.
Review of the various forms of variable remuneration (e.g., cash, shares, stock-based instruments, etc.).	As aforesaid, if the variable annual bonus for a key employee in respect of the measured year exceeds 40 percent of the fixed remuneration - 50 percent of the variable annual bonus is paid in cash and 50 percent - over a period of three years. The deferred variable remuneration may be made, in whole or in part, by way of shares and/or stock-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 stock-based instruments applies to officeholders and key employees and does not apply to other employees of the Bank who are not key employees. The parties responsible for determining the manner of paying the deferred variable remuneration are the Audit Committee and the Board of Directors.

Remuneration Awarded during the Financial Year (REM1)

			A	B	A	B
			For the year ended December 31			
			2018		2017	
			Senior office-holders	Other key emplo-yees	Senior office-holders	Other key emplo-yees
	Remuneration amount		In NIS millions			
1	Fixed remuneration	No. of employees	**18**	**112**	23	104
2=3+5+7		Total fixed remuneration	**31**	**89**	35	86
3		Of which: Cash-based	**31**	**89**	35	86
9	Variable remuneration	No. of employees	**18**	**109**	23	102
10=11+13+15		Total variable remuneration	**9**	**32**	7	27
11		Of which: Cash-based	**9**	**31**	7	27
13		Of which: Shares or other stock-based instruments	**-**[(a)]	**1**	-	-
14		Of which: Deferred	**-**[(a)]	**1**	-	-
17=2+10	Total remuneration		**40**	**121**	42	113

(a) Amount less than NIS 500 thousand.

Special Payments (REM2)

	For the year ended December 31 2018					
	Guaranteed bonuses		Signing bonuses		Severance pay	
	No. of emplo-yees	Total - in NIS millions	No. of emplo-yees	Total - in NIS millions	No. of emplo-yees	Total - in NIS millions
Senior officeholders	**-**	**-**	**4**	**2**	**2**	**1**
Other key employees	**-**	**-**	**2**	**1**	**5**	**6**

	For the year ended December 31 2017					
	Guaranteed bonuses		Signing bonuses		Severance pay	
	No. of emplo-yees	Total - in NIS millions	No. of emplo-yees	Total - in NIS millions	No. of emplo-yees	Total - in NIS millions
Senior officeholders	-	-	5	2	1	1
Other key employees	-	-	-	-	3	5

Deferred Remuneration (REM3)

Deferred Remuneration (REM3)	A	E
	For the year ended December 31 2018	
	Total payable remuneration amount of the outstanding remuneration	Total amount of the deferred remuneration paid during the reporting year
	In NIS millions	
Senior officeholder		
Cash	**-[(a)]**	**-[(a)]**
Shares	**3**	**6**
Cash-based instruments	**-**	**-**
Other	**-**	**-**
Other key employees		
Cash	**1**	**1**
Shares	**7**	**13**
Cash-based instruments	**-**	**-**
Other	**-**	**-**
Total	**11**	**20**

Deferred Remuneration (REM3)	A	E
	For the year ended December 31 2017	
	Total payable remuneration amount of the outstanding remuneration	Total amount of the deferred remuneration paid during the reporting year
	In NIS millions	
Senior officeholder		
Cash	-[(a)]	-
Shares	8	-
Cash-based instruments	-	-
Other	-	-
Other key employees		
Cash	1	1
Shares	20	-
Cash-based instruments	-	-
Other	-	-
Total	29	1

(a) Amount less than NIS 500 thousand.

Additional Information regarding Remuneration

For additional information regarding the remuneration policy, please see Note 23 to the Financial Statements.
For more information regarding officeholder remuneration, please see the section entitled “Salaries of Senior Officeholders” in the Bank’s Corporate Governance Report.

Addenda

Addendum A - Reconciliation of Financial Statements and Regulatory Exposures

Differences between Accounting and Regulatory Scopes of Consolidation and Mapping of Financial Statement Categories with Regulatory Risk Categories (LI1)

	A+B[a]	C	D	E	F	G
	December 31 2018					
		Book value of items that are:				
	Book values as reported in the issued financial statements	Subject to a credit risk framework	Subject to a counterparty credit risk framework	Subject to a securitization framework	Subject to a market risk framework[b]	Not subject to capital requirements nor to deductions from the capital basis
	In NIS millions					
Assets						
Cash and deposits with banks	**81,419**	**80,233**	**1,187**	**-**	**-**	**-**
Securities[c]	**74,571**	**65,158**	**1,880**	**2,645**	**6,764**	**-**
Securities borrowed or purchased under reverse repurchase agreements	**1,257**	**-**	**1,257**	**-**	**-**	**-**
Loans to the public	**274,525**	**274,120**	**405**	**-**	**-**	**-**
Loan loss provision	**(3,352)**	**(3,352)**	**-**	**-**	**-**	**-**
Loans to the public, net	**271,173**	**270,768**	**405**	**-**	**-**	**-**
Loans to governments	**782**	**782**	**-**	**-**	**-**	**-**
Investments in investees	**623**	**463**	**-**	**-**	**-**	**160**
Buildings and equipment	**2,853**	**2,853**	**-**	**-**	**-**	**-**
Intangible assets and goodwill	**17**	**-**	**-**	**-**	**-**	**17**
Assets in respect of derivatives[d]	**12,750**	**-**	**12,750**	**-**	**12,702**	**-**
Other assets	**6,642**	**6,522**	**-**	**-**	**-**	**120**
Assets held for sale	**8,570**	**8,570**	**-**	**-**	**-**	**-**
Total assets	**460,657**	**435,349**	**17,479**	**2,645**	**19,466**	**297**
Liabilities						
Deposits by the public	**364,591**	**-**	**-**	**-**	**-**	**364,591**
Deposits by banks	**5,210**	**-**	**-**	**-**	**-**	**5,210**
Deposits by the Israeli government	**709**	**-**	**-**	**-**	**-**	**709**
Securities loaned or sold under agreements to repurchase	**541**	**-**	**-**	**-**	**-**	**541**
Bonds, capital notes and subordinated bonds	**17,798**	**-**	**-**	**-**	**-**	**17,798**
Liabilities in respect of derivative instruments	**12,089**	**-**	**12,089**	**-**	**12,072**	**-**
Other liabilities	**14,780**	**-**	**-**	**-**	**-**	**14,780**
Held for sale liabilities	**8,778**	**-**	**-**	**-**	**-**	**8,778**
Total liabilities	**424,496**	**-**	**12,089**	**-**	**12,072**	**412,407**

(a) The Bank's accounting consolidation scope and regulatory consolidation scope are one and the same.
(b) The amounts do not include balances used in the calculation of foreign exchange risk, including structural positions in foreign currency, for these balances, please see Note 31 to the Financial Statements.
(c) Securities deposited as collateral for activity in derivative instruments with a central clearing agency whose clearinghouse members are subject to both a credit risk framework (for the securities issuer's risk) and a counterparty credit risk framework (for the counterparty credit risk where the securities were deposited as collateral).
(d) Derivative instruments in the trading book subject to both a market risk framework and a counterparty credit risk framework

	A+B[a]	C	D	E	F	G
	December 31 2017					
		Book value of items that are:				
	Book values as reported in the issued financial statements	Subject to a credit risk framework	Subject to a counterparty credit risk framework	Subject to a securiti-zation framework	Subject to a market risk framework [b]	Not subject to capital require-ments nor to deductions from the capital basis
	In NIS millions					
Assets						
Cash and deposits with banks	82,067	81,654	413	-	-	-
Securities[c]	77,299	69,104	2,015	2,692	5,503	-
Securities borrowed or purchased under reverse repurchase agreements	1,161	-	1,161	-	-	-
Loans to the public	271,165	269,409	1,756	-	-	-
Loan loss provision	(3,213)	(3,213)	-	-	-	-
Loans to the public, net	267,952	266,196	1,756	-	-	-
Loans to governments	715	715	-	-	-	-
Investments in investee companies	807	620	-	-	-	187
Buildings and equipment	2,986	2,986	-	-	-	-
Intangible assets and goodwill	16	-	-	-	-	16
Assets in respect of derivatives[d]	9,573	-	9,573	-	9,603	-
Other assets	8,262	8,198	-	-	-	64
Assets held for sale	-	-	-	-	-	-
Total assets	450,838	429,473	14,918	2,692	15,106	267
Liabilities						
Deposits by the public	362,478	-	-	-	-	362,478
Deposits by banks	5,156	-	-	-	-	5,156
Deposits by the Israeli government	452	-	-	-	-	452
Securities loaned or sold under agreements to repurchase	558	-	-	-	-	558
Bonds, capital notes and subordinated bonds	15,577	-	-	-	-	15,577
Liabilities in respect of derivative instruments	9,740	-	9,740	-	9,732	-
Other liabilities	23,324	-	-	-	-	23,324
Total liabilities	417,285	-	9,740	-	9,732	407,545

(a) The Bank's accounting consolidation scope and regulatory consolidation scope are one and the same.

(b) The amounts do not include balances used in the calculation of foreign exchange risk, including structural positions in foreign currency, for these balances, please see Note 31 to the Financial Statements.

(c) Securities deposited as collateral for activity in derivative instruments with a central clearing agency whose clearinghouse members are subject to both a credit risk framework (for the securities issuer's risk) and a counterparty credit risk framework (for the counterparty credit risk where the securities were deposited as collateral).

(d) Derivative instruments in the trading book subject to both a market risk framework and a counterparty credit risk framework

Reconciliation of Regulatory Capital to Balance Sheet (CC2)

	December 31		References to components of regulatory capital
	2018	2017	
	In NIS millions		
Assets			
Cash and deposits with banks	**81,418**	82,067	-
Securities[1]	**74,571**	77,299	-
Of which: Investments in equity securities of financial corporations which do not exceed 10 percent of the financial corporation's equity capital[1]	**422**	310	14
[1]Of which: other securities	**74,149**	76,989	-
Loans to the public	**274,525**	271,165	-
Less: Balances classified as held for sale assets[(a)]	**8,210**	-	-
Provision for loan losses[1]	**(3,352)**	(3,213)	-
[1]Of which: General loan loss provision included in Tier 2[2]	**(2,903)**	(2,704)	12
[1]Of which: Provision for loan losses not included in regulatory capital	**(617)**	(509)	-
[2]Less: Balances classified as held for sale assets[(a)]	**168**	-	-
Loans to the public, net	**271,173**	267,952	-
Loans to governments	**782**	715	-
Investments in investee companies[1]	**623**	807	-
Of which: investments in the equity securities of financial corporations exceeding 10 percent of the financial corporation's equity capital	**97**	251	15
[1]Of which: goodwill	**161**	187	6
Buildings and equipment	**2,853**	2,986	-
Other assets[1]	**6,643**	8,262	-
[1]Of which: deferred tax assets[2]	**4,785**	5,476	-
[2]Of which: deferred tax assets excluding those attributed to timing differences	**2**	2	8
[2]Of which: deferred tax assets attributed to timing differences; whose total exceeds 10 percent of Common Equity Tier 1 capital	**1,306**	1,681	10
[2]Of which: deferred tax assets attributed to timing differences; whose total does not exceed 10 percent of Common Equity Tier 1 capital	**3,530**	3,471	16
Of which: other deferred tax assets pursuant to the transitional provisions, efficiency plan and average curve [2]	**(53)**	322	13
[2]Less: Balances classified as held for sale assets[(a)]	**(73)**	-	-
[1]Of which: other assets	**1,858**	2,786	-
Intangible assets and goodwill[1]	**17**	16	-
[1]Of which: goodwill	**17**	16	6
Securities borrowed or purchased under reverse repurchase agreements	**1,257**	1,161	-
Assets in respect of derivatives	**12,750**	9,573	-
Assets held for sale[(a)]	**8,570**	-	-
Total assets	**460,657**	450,838	-

(a) For additional information, see Note 36F to the Financial Statements.

	December 31		References to components of regulatory capital
	2018	2017	
	In NIS millions		
Liabilities and capital			
Deposits by the public	**364,591**	362,478	-
Deposits by banks	**5,210**	5,156	-
Deposits by governments	**709**	452	-
Bonds and subordinated bonds[1]	**17,798**	15,577	-
[1]Of which subordinated notes not recognized as regulatory capital	**10,229**	7,835	-
[1]Of which: subordinated notes recognized as regulatory capital[2]	**7,569**	7,742	-
[2]Of which: eligible as regulatory capital components	**1,751**	926	11A
[2]Of which: eligible as regulatory capital components and subject to transitional provisions	**5,818**	6,816	11
Other liabilities[1]	**14,780**	23,324	-
[1]Of which: General loan loss provision included in Tier 2[2]	**340**	334	12
[2]Less: Balances classified as held for sale liabilities[(a)]	**(16)**	-	
Securities borrowed or purchased under reverse repurchase agreements	**541**	558	-
Liabilities in respect of derivative instruments[1]	**12,089**	9,740	-
[1]Of which: in respect of credit risk	**17**	35	9
Liabilities held for sale[(a)]	**8,778**	-	
Total liabilities	**424,496**	417,285	-
Non-controlling interests[1]	**856**	386	-
[1]Of which: non-controlling interests attributable to Common Equity Tier 1 Capital	**399**	229	4
[1]Of which: non-controlling interests attributable to Tier 2 Capital[(b)]	**220**	31	5
Total capital attributed to shareholders of the banking corporation[1]	**35,305**	33,167	-
[1]Of which: ordinary share capital	**7,081**	7,110	1
[1]Of which: premium for ordinary shares	**1,087**	1,729	1
[1]Of which: retained earnings	**29,211**	27,341	2
[1]Of which: Unrealized gains (losses) from adjustment of securities available for sale at fair value	**(316)**	77	3
[1]Of which: net losses from adjustments for translation of financial statements	**(77)**	(184)	3
[1]Of which: other reserves	**74**	44	3
[1] Of which: gains (losses) from adjustments in respect of employee benefits included in regulatory capital	**(1,755)**	(2,360)	3
[1] Of which: profits (losses) from adjustments in respect of employee benefits not included in regulatory capital	**-**	(590)	-
Total shareholders' equity	**36,161**	33,553	-
Total liabilities and capital	**460,657**	450,838	-

(a) For additional information, see Note 36F to the Financial Statements.
(b) Of which, approximately NIS 101 million for the issuance of subordinated bonds by Leumi Card.

Main Sources of Differences between Regulatory Exposure Amounts and Carrying Values in Financial Statements (LI2)

		A	B	C	D	E
		December 31 2018				
			Items subject to:			
		Total	Credit risk frame-work	Securiti-zation frame-work	Counter-party credit risk frame-work	Market risk frame-work
		In NIS millions				
1	Total assets according to the regulatory scope of consolidation (according to the LI1 disclosure format)	**460,360**	**435,349**	**2,645**	**17,479**	**19,466**
2	Total liabilities according to the scope of consolidation (according to the LI1 disclosure format)	**12,089**	**-**	**-**	**-**	**12,072**
3	Total amount according to the regulatory scope of consolidation, net	**448,271**	**435,349**	**2,645**	**17,479**	**7,394**
4	Off-balance sheet amounts[(d)]	**139,048**	**39,690**	**-**	**10,722**	**-**
5	Differences caused by differences in offsetting rules, except those already included in Row 2[(a)]	**(9,318)**	**-**	**-**	**(9,318)**	**-**
6	Differences caused by provisions[(b)]	**3,243**	**3,243**	**-**	**-**	**-**
7	Other adjustments[(c)]	**(413)**	**341**	**-**	**-**	**(754)**
8	Exposure amounts taken into account for regulatory purposes	**580,831**	**478,623**[(e)]	**2,645**	**18,883**	**6,640**

		A	B	C	D	E
		December 31 2017				
			Items subject to:			
		Total	Credit risk frame-work	Securiti-zation frame-work	Counter-party credit risk frame-work	Market risk frame-work
		In NIS millions				
1	Total assets according to the regulatory scope of consolidation (according to the LI1 disclosure format)	450,571	429,473	2,692	14,917	15,106
2	Total liabilities according to the scope of consolidation (according to the LI1 disclosure format)	9,740	-	-	-	9,732
3	Total amount according to the regulatory scope of consolidation, net	440,831	429,473	2,692	14,917	5,374
4	Off-balance sheet amounts[(d)]	135,634	45,523	-	9,668	-
5	Differences caused by differences in offsetting rules, except those already included in Row 2[(a)]	(10,495)	-	-	(10,495)	-
6	Differences caused by provisions[(b)]	3,038	3,038	-	-	-
7	Other adjustments[(c)]	(3,139)	(382)	-	-	(2,757)
8	Exposure amounts taken into account for regulatory purposes	565,869	477,653[(e)]	2,692	14,090	2,617

Explanations of Differences between Accounting and Regulatory Exposures Amounts (LIA):

(a) For regulatory purposes, the Bank employs a netting set for derivative transactions, pursuant to Appendix C to Proper Conduct of Banking Business Directive No. 203 when there are netting agreements in effect. When presenting the total derivatives in the balance sheet, no netting is carried out.

(b) Pursuant to Proper Conduct of Banking Business Directive No. 203, the collective provision included in Tier 2 capital is not deducted from the exposures for calculating credit risk.

(c) Netting positions in the trading book and applying coefficients in accordance with the duration method in Proper Conduct of Banking Business Directive No. 208, as well as adjustments for deferred taxes and efficiency plan.

(d) Addition of off-balance sheet items that constitute credit risk (business lines and guarantees), including components of potential future exposure to derivatives volatility.

(e) The difference between the credit exposure amounts is primarily due to the 250 percent weighted amounts included in LI2 and not included in CR4.

Addendum B - Securitization

Securitization Exposures (SECA)

The Bank's securitization exposures, in accordance with the capital adequacy provisions, arise from an investment in the Bank's own (nostro) portfolio.

The Bank is not involved in asset securitization activities, either as originator or as a direct sponsor for the securitization entities.

Asset-backed securities are characterized by wide diversification of borrowers. For some instruments, there are several risk layers, which allow the Bank to be flexible when adapting an investment to its risk appetite.

Most of the Bank's investments in securitized products are a fully backed or backed by implication by the US government. In 2018, the Bank did not invest in synthetic or re-securitized products.

As a rule, investment in securitized products is mainly managed through the banking portfolio.

Risk management of securitized products is carried out with continuous monitoring of the development of risk indicators and testing compliance with restrictions and stress scenarios. Monitoring is carried out by dedicated and independent risk management and control units. In addition, a dedicated periodic discussion takes place, focusing on the overall risk picture of the securitized products with the participation of the relevant parties.

For additional information, please see Note 12 to the Financial Statements.

Description of Securitization Exposures

Securitization Exposures in the banking book[(a)] (SEC1))

		A	B	C	E	F	G	I	J	K
		December 31 2018								
		Banking corporation is acting as originator			Banking corporation is acting as sponsor			Banking corporation is acting as investor		
		Traditional	Synthetic	Subtotal	Traditional	Synthetic	Subtotal	Traditional	Synthetic	Subtotal
		In NIS millions								
1	Retail (total), of which:	-	-	-	-	-	-	**6,643**	-	**6,643**
2	Housing mortgage	-	-	-	-	-	-	**6,635**	-	**6,635**
3	Credit cards	-	-	-	-	-	-	**8**	-	**8**
6	Wholesale (total), of which:	-	-	-	-	-	-	**4,386**	-	**4,386**
7	Loans to corporations	-	-	-	-	-	-	**2,211**	-	**2,211**
8	Commercial mortgage	-	-	-	-	-	-	**2,175**	-	**2,175**
11	Re-securitization	-	-	-	-	-	-	-	-	-

		A	B	C	E	F	G	I	J	K
		December 31 2017								
		Banking corporation is acting as originator			Banking corporation is acting as sponsor			Banking corporation is acting as investor		
		Traditional	Synthetic	Subtotal	Traditional	Synthetic	Subtotal	Traditional	Synthetic	Subtotal
		In NIS millions								
1	Retail (total), of which:	-	-	-	-	-	-	5,125	-	5,125
2	Housing mortgage	-	-	-	-	-	-	5,125	-	5,125
3	Credit cards	-	-	-	-	-	-	-	-	-
6	Wholesale (total), of which:	-	-	-	-	-	-	3,757	-	3,757
7	Loans to corporations	-	-	-	-	-	-	1,585	-	1,585
8	Commercial mortgage	-	-	-	-	-	-	2,153	-	2,153
11	Re-securitization	-	-	-	-	-	-	19	-	19

(a) Disclosure balances reflect credit exposure (EAD) after other than temporary provisions for loan losses or impairments, before the effect of credit risk mitigators.

Securitization Exposures in the Trading Book (SEC2)

		A	B	C	E	F	G	I	J	K
		December 31 2018								
		Banking corporation is acting as originator			Banking corporation is acting as sponsor			Banking corporation is acting as investor		
		Tradi-tional	Synthe-tic	Subtotal	Tradi-tional	Synthe-tic	Subtotal	Tradi-tional	Synthe-tic	Subtotal
		In NIS millions								
1	Retail (total), of which:	-	-	-	-	-	-	**137**	-	**137**
2	Housing mortgage	-	-	-	-	-	-	**52**	-	**52**
3	Credit cards	-	-	-	-	-	-	**7**	-	**7**
4	Other retail exposures	-	-	-	-	-	-	**78**	-	**78**
6	Wholesale (total), of which:	-	-	-	-	-	-	**134**	-	**134**
7	Loans to corporations	-	-	-	-	-	-	**134**	-	**134**

		A	B	C	E	F	G	I	J	K
		December 31 2017								
		Banking corporation is acting as originator			Banking corporation is acting as sponsor			Banking corporation is acting as investor		
		Tradi-tional	Synthe-tic	Subtotal	Tradi-tional	Synthe-tic	Subtotal	Tradi-tional	Synthe-tic	Subtotal
		In NIS millions								
1	Retail (total), of which:	-	-	-	-	-	-	133	-	133
2	Housing mortgage	-	-	-	-	-	-	59	-	59
3	Credit cards	-	-	-	-	-	-	4	-	4
4	Other retail exposures	-	-	-	-	-	-	70	-	70
6	Wholesale (total), of which:	-	-	-	-	-	-	135	-	135
7	Loans to corporations	-	-	-	-	-	-	135	-	135

Calculation of Capital Requirements

Securitization Exposures in the Banking Book and Associated Regulatory Capital Requirements – Bank Acting as Originator or as Sponsor (SEC3)

As at December 31 2018 and December 31 2017, the Bank is not involved in asset securitization activities, either as originator or sponsor for other entities.

Securitization Exposures in the Banking Book and Associated Capital Requirements – Bank Acting as Investor[(a)] (SEC4)

		A	B	C	D	E	H	I	L	M	P	Q
		December 31 2018										
		Exposure values according to the RW rate [(a)]					Exposure values according to the regulatory approach		RWA according to the regulatory approach		Capital charge after the implementation of the ceiling	
		Up to 20%	20- 50%	50-100%	100-1250%	1250%	SA/SSF A	1250%	SA/SSF A	1250%	SA/SSF A	1250%
		In NIS millions										
1	Total exposures	**2,617**	**28**	**-**	**-**	**-**	**2,645**	**-**	**411**	**-**	**57**	-
2	Traditional securitization[1]	**2,617**	**28**	**-**	**-**	**-**	**2,645**	**-**	**411**	**-**	**57**	-
3	[1]Of which: securitization[2]	**2,617**	**28**	**-**	**-**	**-**	**2,645**	**-**	**411**	**-**	**57**	-
4	[2]Of which: retail basis	**252**	**-**	**-**	**-**	**-**	**252**	**-**	**51**	**-**	**7**	-
5	[2]Of which: Wholesale	**2,365**	**28**	**-**	**-**	**-**	**2,393**	**-**	**360**	**-**	**50**	-
6	[1]Of which: re-securitization[2]	-	-	-	-	-	-	-	-	-	-	-
7	[2]Of which: senior	-	-	-	-	-	-	-	-	-	-	-

		A	B	C	D	E	H	I	L	M	P	Q
		December 31 2017										
		Exposure values according to the RW rate [(a)]					Exposure values according to the regulatory approach		RWA according to the regulatory approach		Capital charge after implementation of the ceiling	
		Up to 20%	20- 50%	50-100%	100-1250%	1250%	SA/SSF A	1250%	SA/SSF A	1250%	SA/SSF A	1250%
		In NIS millions										
1	Total exposures	2,514	177	-	-	-	2,692	-	441	-	61	-
2	Traditional securitization[1]	2,514	177	-	-	-	2,692	-	441	-	61	-
3	[1]Of which: securitization[2]	2,514	158	-	-	-	2,673	-	433	-	60	-
4	[2]Of which: retail basis	903	-	-	-	-	903	-	32	-	5	-
5	[2]Of which: Wholesale	1,611	158	-	-	-	1,770	-	401	-	55	-
6	[1]Of which: re-securitization[2]	-	19	-	-	-	19	-	8	-	1	-
7	[2]Of which: senior	-	19	-	-	-	19	-	8	-	1	-

(a) Disclosure balances reflect credit exposure (EAD) after other than temporary provisions for loan losses or impairments, before the effect of credit risk mitigators including guarantees.

Legend

Key Metrics	KM
Overview	OV
Capital Composition	CC
Leverage Ration	LR
Credit Risk	CR
Counterparty Credit Risk	CCR
Market Risk	MR
Liquidity	LIQ
Remuneration	REM
Linkages	LI
Securitization	SEC