Translation of Immediate Report

T125

Public

Bank Leumi Le-Israel B.M.

Registration No. 520018078

Securities of the Corporation are listed on The Tel Aviv Stock Exchange

Abbreviated Name: Leumi

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Transmission Date: November 7 2019

Reference: 2019-01-095919

To: Israel Securities Authority (www.isa.gov.il)

The Tel Aviv Stock Exchange (www.tase.co.il)

Immediate Report of Rating of Bonds/Rating of a Corporation, or of Withdrawal of Rating

On November 7 2019, Standard & Poor's Maalot published the following:

A rating report/update notice:

1. Rating report or notice

   Rating of the corporation: S&P Maalot ilAAA ___ *stable* _______
   Comments/Nature of Notice: *Reiteration of rating*

   Ratings history for the 3 years preceding the date of the rating/notice:

Date	Subject of Rating	Rating	Comments/ Substance of Notice
November 7, 2019	Bank Leumi Le-Israel Ltd.	*S&P Maalot ilAAA ___ stable ___*	Reiteration of rating
July 11 2018	Bank Leumi Le-Israel Ltd.	*S&P Maalot ilAAA ___ stable ___*	Reiteration of rating
October 24 2017	Bank Leumi Le-Israel Ltd.	*S&P Maalot ilAAA ___ stable*	Reiteration of rating
December 21 2016	Bank Leumi Le-Israel Ltd.	*S&P Maalot ilAAA ___ stable*	Reiteration of rating

Explanation: As part of the ratings history one should only provide the details of the rating history of the rating agency which is the subject matter of the immediate report.

2. Rating of the corporation's bonds:

Security name & type	TASE Security No.	Rating agency	Current rating	Comments / nature of notice
Leumi Sub. Bonds 400	6040331	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating ____________*
Leumi Sub. Bonds 401	6040380	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating ____________*
Leumi Sub. Bonds 402	6040398	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating ____________*
Leumi Sub. Bonds 403	6040430	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating ____________*
Leumi Sub. Bonds 404	--------	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*First Rating ____________*
Bonds Series 177	6040315	*S&P Maalot*	*S&P Maalot ilAAA ___ stable*	*Reiterated rating ____________*
Bonds Series 178	6040323	*S&P Maalot*	*S&P Maalot ilAAA ___ stable*	*Reiterated rating ____________*
Bonds Series 179	6040372	*S&P Maalot*	*S&P Maalot ilAAA ___ stable*	*Reiterated rating ____________*
Bonds Series 180	6040422	*S&P Maalot*	*S&P Maalot ilAAA ___ stable*	*Reiterated rating ____________*
Sub. Bonds N	6040299	*S&P Maalot*	*S&P Maalot ilAA+ ___ stable*	*Reiterated rating ____________*
Capital Notes Series 200	6040141	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating ____________*
Capital Notes Series 201	6040158	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating ____________*
Capital Notes Series 300	6040257	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating ____________*
Capital Notes Series 301	6040265	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating ____________*

Rating history in the 3 years prior to the rating/notice date:

Security name & type	TASE Security No.	Date	Type of rated security	Rating agency	Current rating	Comments / nature of notice
Leumi Sub. Bonds 400	6040331	*July 11 2019*	*Contingent subordinated bonds*	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating*
Leumi Sub. Bonds 400	6040331	*Nov. 7 2018*	*Contingent subordinated bonds*	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating*
Leumi Sub. Bonds 400	6040331	*Oct. 24 2017*	*Contingent subordinated bonds*	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating*
Leumi Sub. Bonds 401	6040380	*July 11 2019*	*Contingent subordinated bonds*	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating*
Leumi Sub. Bonds 401	6040380	*Nov. 7 2018*	*Contingent subordinated bonds*	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating*
Leumi Sub. Bonds 401	6040380	*May 7 2018*	*Contingent subordinated bonds*	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*First rating*
Leumi Sub. Bonds 402	6040398	*July 11 2019*	*Contingent subordinated bonds*	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating*
Leumi Sub. Bonds 402	6040398	*Nov. 7 2018*	*Contingent subordinated bonds*	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating*
Leumi Sub. Bonds 402	6040398	*July 5 2018*	*Contingent subordinated bonds*	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*First rating*
Leumi Sub. Bonds 403	6040430	*July 11 2019*	*Contingent subordinated bonds*	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating*
Leumi Sub. Bonds 403	6040430	*Jan. 29 2019*	*Contingent subordinated bonds*	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*First rating*
Bonds Series 177	6040315	*July 11 2019*	*Senior unsecured bonds*	*S&P Maalot*	*S&P Maalot ilAAA ___ stable*	*Reiterated rating*
Bonds Series 177	6040315	*Nov. 7 2018*	*Senior unsecured bonds*	*S&P Maalot*	*S&P Maalot ilAAA ___ stable*	*Reiterated rating*
Bonds Series 177	6040315	*Oct. 24 2017*	*Senior unsecured bonds*	*S&P Maalot*	*S&P Maalot ilAAA ___ stable*	*Reiterated rating*
Bonds Series 177	6040315	*Dec. 21 2016*	*Senior unsecured bonds*	*S&P Maalot*	*S&P Maalot ilAAA ___ stable*	*Reiterated rating*
Bonds Series 178	6040323	*July 11 2019*	*Senior unsecured bonds*	*S&P Maalot*	*S&P Maalot ilAAA ___ stable*	*Reiterated rating*
Bonds Series 178	6040323	*November 7 2018*	*Senior unsecured bonds*	*S&P Maalot*	*S&P Maalot ilAAA ___ stable*	*Reiterated rating*
Bonds Series 178	6040323	*Oct. 24 2017*	*Senior unsecured bonds*	*S&P Maalot*	*S&P Maalot ilAAA ___ stable*	*Reiterated rating*

Bonds Series 178	6040323	*Dec. 21 2016*	*Senior unsecured bonds*	*S&P Maalot*	*S&P Maalot ilAAA ___ stable*	*Reiterated rating*
Bonds Series 179	6040372	*July 11 2019*	*Senior unsecured bonds*	*S&P Maalot*	*S&P Maalot ilAAA ___ stable*	*Reiterated rating*
Bonds Series 179	6040372	*Nov. 7 2018*	*Senior unsecured bonds*	*S&P Maalot*	*S&P Maalot ilAAA ___ stable*	*Reiterated rating*
Bonds Series 179	6040372	*May 31 2018*	*Senior unsecured bonds*	*S&P Maalot*	*S&P Maalot ilAAA ___ stable*	*First rating*
Bonds Series 180	6040422	*July 11 2019*	*Senior unsecured bonds*	*S&P Maalot*	*S&P Maalot ilAAA ___ stable*	*Reiterated rating*
Bonds Series 180	6040422	*Jan. 17 2019*	*Senior unsecured bonds*	*S&P Maalot*	*S&P Maalot ilAAA ___ stable*	*First rating*
Sub. Bonds N	6040299	*July 11 2019*	*Senior unsecured bonds*	*S&P Maalot*	*S&P Maalot ilAAA ___ stable*	*Reiterated rating*
Sub. Bonds N	6040299	*Nov. 7 2018*	*Subordinated bonds*	*S&P Maalot*	*S&P Maalot ilAAA ___ stable*	*Reiterated rating*
Sub. Bonds N	6040299	*Oct. 24 2017*	*Subordinated bonds*	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating*
Sub. Bonds N	6040299	*Dec. 21 2016*	*Subordinated bonds*	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating*
Capital Notes Series 200	6040141	*July 11 2019*	*Subordinated bonds*	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating*
Capital Notes Series 200	6040141	*Nov. 7 2018*	*Subordinated capital notes*	*S&P Maalot*	*S&P Maalot ilAAA+ ___ stable*	*Reiterated rating*
Capital Notes Series 200	6040141	*Oct. 24 2017*	*Subordinated capital notes*	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating*
Capital Notes Series 200	6040141	*Dec. 21 2016*	*Subordinated capital notes*	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating*
Capital Notes Series 201	6040158	*July 11 2019*	*Subordinated capital notes*	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating*
Capital Notes Series 201	6040158	*Nov. 7 2018*	*Subordinated capital notes*	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating*
Capital Notes Series 201	6040158	*Oct. 24 2017*	*Subordinated capital notes*	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating*
Capital Notes Series 201	6040158	*Dec. 21 2016*	*Subordinated capital notes*	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating*
Capital Notes Series 300	6040257	*July 11 2019*	*Subordinated capital notes*	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating*
Capital Notes Series 300	6040257	*Nov. 7 2018*	*Subordinated capital notes*	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating*

Capital Notes Series 300	6040257	*Oct. 24 2017*	*Subordinated capital notes*	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating*
Capital Notes Series 300	6040257	*Dec. 21 2016*	*Subordinated capital notes*	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating*
Capital Notes Series 301	6040265	*July 11 2019*	*Subordinated capital notes*	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating*
Capital Notes Series 301	6040265	*Nov. 7 2018*	*Subordinated capital notes*	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating*
Capital Notes Series 301	6040265	*Oct. 24 2017*	*Subordinated capital notes*	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating*
Capital Notes Series 301	6040265	*Dec. 21 2016*	*Subordinated capital notes*	*S&P Maalot*	*S&P Maalot ilAA ___ stable*	*Reiterated rating*

Explanation: As part of the ratings history one should only provide the details of the rating history of the rating agency which is the subject matter of the immediate report.

Attached is the Ratings Report:
Bank Leumi Ratification of rating November7 2019_isa.pdf

Standard & Poor's has reiterated the Bank's long-term IDR at ilAAA and reiterated the outlook as Stable.

The report was signed on behalf of the corporation, in accordance with Regulation 5 of the Securities (Periodic and Immediate Reports) Regulations, 1970, by Mr. Omer Ziv, Head of the Finance Division of the Bank.

Reference numbers of previous documents on this subject (this reference does not constitute inclusion by way of reference):

Date on which the format of this form was updated: October 29 2019

Note: English translations of Immediate Reports of Bank Leumi are for convenience purposes only. In case of any discrepancy between the English translation and the Hebrew original, the Hebrew version shall prevail. The original Hebrew version is available on the distribution website of the Israel Securities Authority: http://www.magna.isa.gov.il

Name of Electronic Reporter: Livnat Ein-Shay (Adv.), Position: Secretary

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Bank Leumi Le-Israel B.M.

November 7 2019

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Bank Leumi of Israel Ltd.

Issuer's rating reiteration	ilAAA/Stable

Strengths and weaknesses

Strengths	Weaknesses
• Strong business position and brand as one of the two largest Israeli banking groups, with strong presence in all lines of business and in digital banking. • Ongoing improvement in efficiency ratios. • Extensive depositor base that supports adequate funding and liquidity ratios. • Indicators reflecting high quality of assets.	• Regulatory attempts to restrict the market share, as reflected in the forced divestment from the credit card company. • Concentration risk due to exposure to the domestic real estate sector. • Restricted ability to diversify or increase revenues from commissions.

Rating outlook: Stable

The stable rating outlook reflects a limited probability for negative rating action in the next 12-24 months. The Bank's rating already takes into account the advantages of the stable business environment in Israel which we predict. We expect that the Bank's business and financial profile and its risk profile will remain stable in the near future.

The negative scenario

Pressures to take negative rating action may arise if the Israeli economy will deteriorate, particularly in the real estate sector. Such deterioration may stem from global or local economic pressures, or from a real escalation in regional geopolitical conditions. Furthermore, negative rating action may arise from a significant deterioration in the quality of assets or the operating risks that the activity in the USA involves, or from legislative or regulatory changes, such as the legislation that triggered the Bank's selling its credit card company, to the extent that those factors will cause a significant deterioration in the Bank's business position.

Main considerations for rating

We expect that Bank Leumi will continue to maintain good positioning and extensive business distribution that will be supported by the business environment. The forced divestment of the subsidiary Leumi Card (MAX – after rebranding) may slightly reduce the diversity and scope of non-interest revenues. However, this will have a limited impact on the business positioning the next three-four years in terms of loss of market share. On June 30 2019, the Bank's CEO, Ms. Rakefet Russak-Aminoach announced her intention to step down as CEO. Mr. Hanan Friedman, the former Head of the Strategy and Regulation Division was appointed Bank's President and CEO. We believe that Bank's management is experienced and professional, and do not think that those changes will have a material impact on the Bank's strategy. We estimate that the Bank's capital profile is strong and predict that its Risk Adjusted Capital (RAC) ratio (before adjustments) will remain higher than 10% in the next few years. The capital profile will also be supported by the moderate growth of Bank's assets despite the increase in dividend distribution and the Bank's buyback plan (buyback of 2% of the share capital at an amount of up to NIS 700 million dollars in 2019). Nevertheless, and despite sound asset quality indicator, we estimate that the risk profile of Bank Leumi is weaker than that of peers operating in countries with a similar economic risk. This distinction points to the rather concentrated nature of the Israeli economy and sensitivity to tail risks associated with sectoral concentration in the real estate market. In our base scenario, we estimate that the economic risks associated with regional geopolitical tensions will remain limited and manageable for the Bank.

We assess the Bank's funding profile as 'average' since it is supported by a large and granular deposit base. We assess the Bank's liquidity as 'adequate' since we believe that its inventory of liquid assets comfortably covers its liquidity needs, reducing reliance on short-term wholesale funding.

The Bank's Issuer Credit Rating (ICR) is one notch above its Stand-Alone Credit Profile (SACP), since we estimate that there is a fairly high likelihood that extraordinary support will be rendered by the State of Israel (AA-/Stable/A-1+), where required. We classify Bank Leumi as a systematically important bank and the State of Israel as supportive towards the domestic banking sector.

Anchor: Reflects the focus on the Israeli activity

S&P Global's rating methodology for banking institutions is based on our assessment of the Israeli banking sector from a global perspective (BICRA –Banking Industry Country Risk Assessment), as an anchor for bank ratings, i.e. a starting point rating. This assessment combines the economic risk assessment and the sectoral risk assessment. The BICRA score of the Israeli banking sector is 3 on a 1 to 10 scale, with 1 reflecting the lowest risk (a BICRA score of 3 comprises a score of 3 for the economic risk and a score of 4 of the sectoral risk). We base our assessment on the geographical distribution of the Bank's credit portfolio, of which 92% relates to Israel and 8% relates to the USA as of June 30, 2019. We estimate that this distribution shall remain stable over the next 24 months.

We view the domestic economic factors as supporting the banking sector. The high income, sustained growth and moderate leverage in the Israeli economy supported the banking sector and enabled business opportunities and growth, increase in profitability and stronger asset quality. Despite the banks' large exposure to the real estate market, we believe that the risk arising from this exposure has become more moderate as a consequence of the stabilization of prices in the last couple of years and as a result of the regulator's macroprudential measures.

As to the sectoral risk, the Israeli banking sector has an adequate institutional framework and it is supported by a high and stable share of core retail deposits. Attempts were made to spur competition in retail credit and credit to small and medium businesses – segments in which the large banks retain their dominant position. Recently, the two largest banks had to divest their credit card companies; however, it is still too early to estimate how competition will develop. In our opinion, Israeli banks are well placed to withstand the changes in competition. However, in the near future these changes will continue to threaten both banks and non-bank players. The banks and the regulator focus more of their attention on operational risks, such as information security and cyber threats. We believe that the Israeli banking system tackles these issues in a thorough manner, supported by an extensive regulatory framework and skilled manpower.

Table 1.

Bank Leumi Le-Israel B.M. Key Figures (Mil. ILS)

	YTD June 2019	2018	2017	2016	2015
Adjusted assets	467,125	459,901	450,822	438,586	416,481
Customer loans (gross)	281,217	275,307	271,880	266,092	265,523
Adjusted common equity	34,164	33,501	30,269	29,301	27,948
Operating revenues	7,321	13,535	13,388	12,934	13,404
Noninterest expenses	3,896	8,115	8,415	8,580	8,831
Core earnings	2,035	3,295	3,141	2,787	2,753

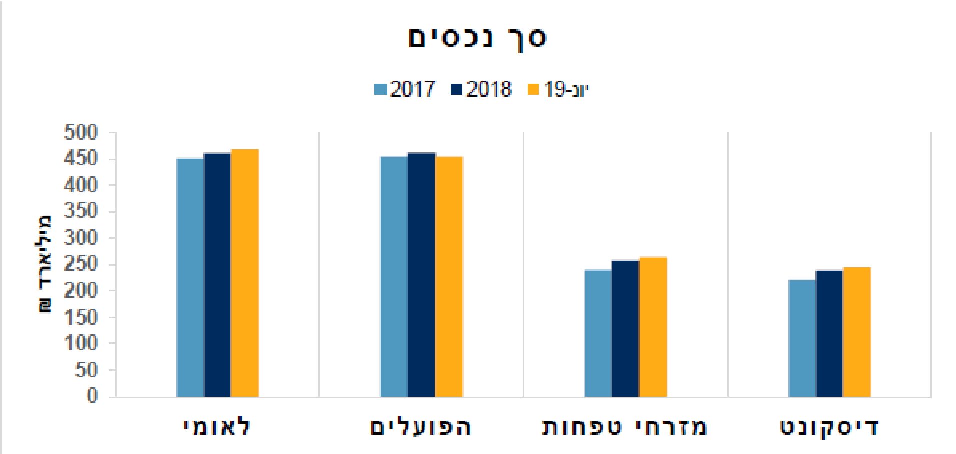
Data are based on S&P Global Ratings adjusted number and ratios

Business position: One of the two largest banks in the Israeli economy

Our assessment of the Bank's business position as 'strong' reflects its leading position as one of the Israel's two largest banking groups. As of June 30, 2019, Leumi's total assets amounted to NIS 468 billion, with a stable market share of 29% of total public's deposits and bank credit in the Israeli economy in recent years. Bank Leumi is supported by a high level of brick & mortar branches and forward-looking innovation, with 177 retail branches, 24 business branches charged with the activity of middle-market commercial companies and the Leumi-Tech business center, through which the Bank runs its activity with high-tech companies (a significant market share in the high-tech sector, which is still moderate in size).

Bank Leumi has a diversified mix of business lines supported by the Bank's presence in all segments of the Israeli banking industry, including complementary activities such as services to capital market investors and investment banking with a focus on equity investments in nonfinancial companies. We believe this wide diversification suggests that the Bank handles industry challenges better than peers facing a similar sectoral risk, such as smaller banks and banks in Spain and the Czech Republic – and mitigates its high geographic concentration.

Chart 1



Source: S&P Global Ratings

We expect the Bank to record higher-than-average sectoral lending growth, especially in mortgages and corporate credit segments, given the Bank's temporary capital advantage, which renders it with a greater room to maneuver than that of some of its peers which are more hard-pressed for capital. Currently, the Bank aims to maintain its position through both traditional and alternative channels. In particular, it targets younger clients, through its mobile banking platform Pepper, and is promoting its payment app Pay and its digital mortgage and digital investment management platform Videa.

Moreover, as a consequence of the tax investigation by US authorities and stricter global regulation, risk appetite toward large-scale acquisitions or international expansion has decreased, with the Bank mainly focusing on existing activity in the USA. The US subsidiary still accounts for a small portion of the Bank's overall activity (less than 10% of the Bank's revenues and profits in the first half of 2019), and competition makes the expansion of this activity challenging.

In 2018, the Bank sold 15% of its stake in its US subsidiary to two strategic investors, in order to utilize their expertise with a view to expand the field of middle-market corporate lending in the US. However, we believe that the fact that the US subsidiary focuses on the commercial real estate sector and on strategies for providing niche commercial loans – which together account for most of the loan portfolio - constitutes a weakness as compared to other regional banks in the USA.

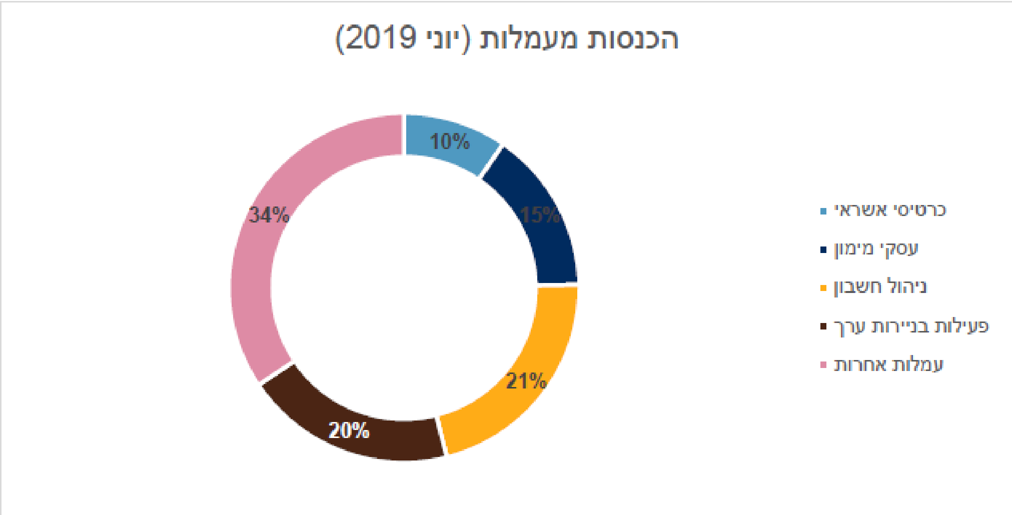
On the other hand, we believe the domestic market's maturity and highly competitive nature, in combination with constant scrutiny of banks' activities by regulators and political groups, might restrict the Bank's growth. The divestment of the Bank's credit card subsidiary, Leumi Card, as required by the regulator, may have some adverse impact on its business position in the next three-to-four years, since the bank may lose market share in consumer lending and markedly decrease the amount and diversity of non-interest revenue. During the two years prior to the divestment, Leumi Card's activity accounted for 3% of the Bank's total lending and 5% of the Group's net income.

Bank Leumi and the Azrieli Group sold Leumi Card to the US-based investment fund Warburg Pincus. Leumi Card's value as per the transaction is NIS 2.5 billion (30% above its carrying amount); this amount will be paid in three installments over three years.

In the first half of 2019, revenues from clearing fees constituted 10% of the Bank's total fees revenues. The sale will have some impact on fees revenues. At this stage, it is still not clear how much of this loss will be recovered by interchange fees, card fees and distribution fees, since the Bank now works with multiples credit card companies. Therefore, it is too early to estimate whether the divestment of Leumi Card will significantly undermine Bank Leumi prominent position in consumer and retail banking in the long run.

Mr. Hanan Friedman, who was lately appointed as the Bank's President and CEO, will replace Ms. Rakefet Russak-Aminoach, who served as CEO since May 2012. Prior to his appointment as the Bank's President and CEO, Mr. Friedman headed the Strategy and Regulation Division, and was significantly involved in the Bank's strategic initiatives, such as digital banking and processes streamlining. We believe that Bank's management is experienced and professional and expect that the Bank will continue to implement its strategy. The Bank has a robust mechanism of balances and balances embedded into its decision-making process, with independent directors that contribute to its strategy.

Chart 2



Source: S&P Global Ratings

Table 2.

Bank Leumi Le-Israel B.M. Business Position (%)

	YTD June 2019	2018	2017	2016	2015
Total revenues from business line (Mil ILS)	7,321	13,580	13,480	13,000	13,592
Commercial banking/total revenues from business line	42.0	44.6	40.8	38.4	39.6
Retail banking/total revenues from business line	26.3	35.7	35.9	36.9	37.0
Commercial & retail banking/total revenues from business line	68.3	80.3	76.8	75.3	76.6
Other revenues/total revenues from business line	31.7	19.7	23.2	24.7	23.4
Return on average common equity (%)	11.3	9.5	9.8	9.3	10.3

Data are based on S&P Global Ratings adjusted number and ratios

Capital and earnings: maintaining a moderate increase in risk assets

We estimate that the Bank's Risk Adjusted Capital (RAC) ratio will be above 10% in the next couple of years, which supports our estimate of the Bank's capital and earnings as 'strong'. Our estimate of the Risk Adjusted Capital is supported by the revision to the Group's BICRA score from '4' to '3' reflecting our view of the supportive domestic environment, which lowered the risk weights we apply to the RAC's risk exposure.

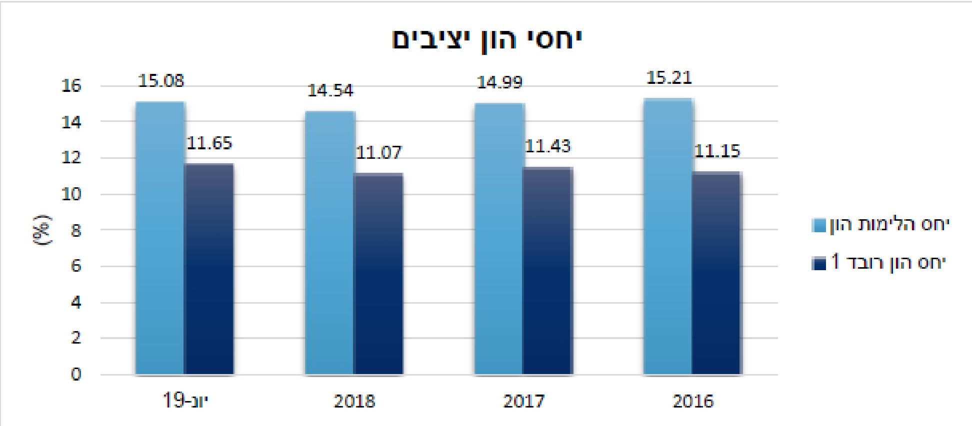
We believe that the Bank's moderate capital generation capability does not present a major rating risk. This is because management does not aim to aggressively increase the Bank's credit portfolio, and we expect real credit risk costs to remain significantly below our normalized cost estimate in the next couple of years.

Our outlook for the Risk Adjusted Capital (RAC) takes into account the one-off distribution by way of share buyback plan of NIS 700 million in 2019, of excess capital arising from the sale of Leumi Card and ensuing release of risk weighted assets. Our base scenario also takes into account the Bank's move toward a shareholder friendly policy, through dividend distributions totaling 40% of quarterly earnings. Nevertheless, we believe that the Bank will maintain some flexibility in its distribution policy, since it operates without a controlling shareholder.

Our calculation of the Risk Adjusted Capital (RAC) does not take into account significant changes in the actuarial valuation of the liabilities for employees' pension. We believe that the Bank's regulatory capital ratio will be impacted to a larger extent than that of its principal domestic peer by changes in the consumer price index and the discount rates, given its liability for employees' pension. This is despite the fact that the regulator moderated this impact by allowing the Bank to use a rolling-eight-quarter discount rate in its calculation of its pension obligations.

Israeli banks, unlike their counterparts in many developed countries, use the conservative standardized approach in calculating risk-weighted assets, as dictated by the Bank of Israel, rather than advanced models. This results in materially lower regulatory capital ratios compared with those of their foreign peers (for instance, an 11.65% tier 1 capital ratio as of June 30, 2019), and a relatively low capital surplus above the regulatory minimum threshold. The Bank aims to reach a Tier 1 capital ratio of 50 base points above the 10.5% regulatory threshold in the next few years. However, we do not consider this to be a risk, since the regulator is satisfied with these narrow margins. We do not believe that this will change in the near future.

Chart 3



Source: S&P Global Ratings

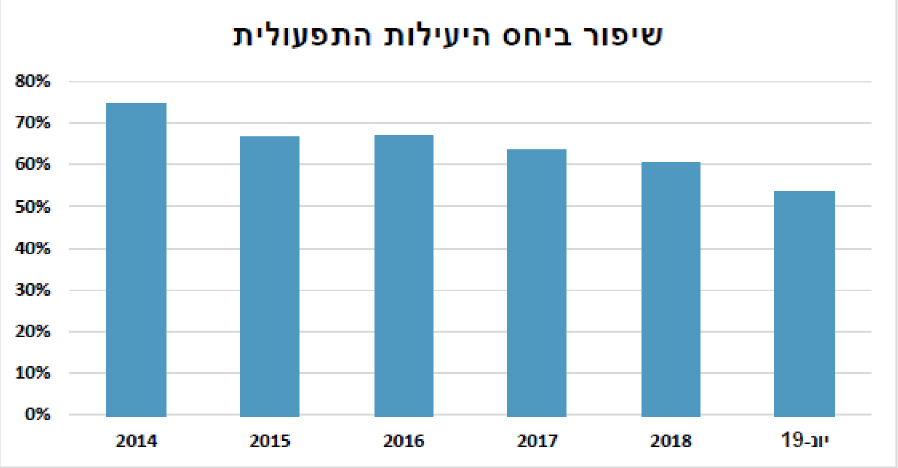
We predict some acceleration in credit growth, which is currently fairly moderate (predicted annual growth of 5% in 2019), especially in middle market, corporate and real estate sectors as the Bank's capital buffer over minimum regulatory requirements continues to expand.

We estimate that credit losses shall continue to increase from their current low levels, which we view as unsustainable in the next couple of years, because the Bank will record fewer debt recoveries. We expect the cost-of-risk cost ratio to stabilize at 30 base points over 2019-2020, being at 19 base points in the first half of 2019.

Given the high concentration of mortgages and real estate lending in the overall business mix, adverse developments in the real estate market – although not factored into our base scenario – may pose a risk to the capital forecast. We also expect that the continued low interest rate environment will continue to strain the Bank's overall interest margins. However, the underlying core margin will benefit moderately from the shifting business mix into higher-margin sectors.

The continued improvement in operational efficiency is a key management target, and the Bank has made progress in achieving that target. In recent years, the Bank implemented streamlining plans resulting in a substantial reduction the number of employees and an improvement in operational efficiency. The cost income ratio has improved from 70% in 2013 to 53% in the first half of 2019. The trade union of the Bank's employees has historically achieved above-industry-average wage agreements, however, and the Bank reached a new wage agreement with workers in the first half of 2019. In the third quarter of 2019, the Bank announced the acceleration of the process of manpower cuts. Although efficiency-positive in the long term, this could give rise to one-off expenses in 2019, in turn reducing annual profits. In the first quarter of 2019, the Bank centralized processes and operational activities in a new operations division, which should streamline back-office operations, and in the third quarter of 2019 it launched relocation of its headquarters outside Tel Aviv. Making further inroads in operational efficiency will also depend on the Bank leveraging significant IT investment of the past few years, both in core banking systems and front ends interfaces, such as Pepper. We also expect some of the profits from the Leumi Card divestment to be invested in IT systems enhancement.

Chart 4



Source: S&P Global Ratings

Table 3.

Bank Leumi Le-Israel B.M. Capital and Earnings (%)

	YTD June 2019	2018	2017	2016	2015
Tier 1 capital ratio	11.7	11.1	11.4	11.2	9.6
S&P RAC ratio before diversification	N/A	9.1	9.4	9.1	9.0
S&P RAC ratio after diversification	N/A	8.3	8.4	8.4	8.9
Adjusted common equity/total adjusted capital	100.0	100.0	100.0	100.0	100.0
Net interest income/operating revenues	62.6	65.7	60.1	58.2	53.1
Fee income/operating revenues	N/A	28.8	30.3	30.7	30.5

	YTD June 2019	2018	2017	2016	2015
Market-sensitive income/operating revenues	N/A	5.0	6.9	9.9	11.9
Noninterest expenses/operating revenues	53.2	60.0	62.9	66.3	65.9
Preprovision operating income/average assets	1.5	1.2	1.1	1.0	1.1
Core earnings/average managed assets	0.9	0.7	0.7	0.7	0.7

N/A – not applicable. Data are based on S&P Global Ratings adjusted number and ratios.

Table 4.

Bank Leumi Le-Israel B.M. RACF [Risk-Adjusted Capital Framework] Data (Mil. ILS)

	Exposure*	Basel III RWA	Average Basel III RW (%)	S&P Global RWA	Average S&P Global RW (%)
Credit risk					
Government and central banks	130,096	5,511	4	2,088	2
Of which regional governments and local authorities	12,416	3,665	30	448	4
Institutions and CCPs	26,030	4,821	19	7,705	30
Corporate	183,560	173,224	94	173,981	95
Retail	127,437	80,354	63	70,094	55
Of which mortgage	80,804	45,083	56	29,913	37
Securitization§	2,015	411	20	411	20
Other assets†	9,218	22,316	242	20,277	220
Total credit risk	478,356	286,637	60	274,556	57
Credit valuation adjustment					
Total credit valuation adjustment	--	1,518	--	0	--
Market risk					
Equity in the banking book	7,305	682	9	59,052	808
Trading book market risk	--	6,295	--	9,442	--
Total market risk	--	6,976	--	68,493	--
Operational risk					
Total operational risk	--	22,713	--	25,378	--

	Basel III RWA	S&P Global RWA	% of S&P Global RWA
Diversification adjustments			
RWA before diversification	317,844	368,428	100
Total Diversification/ Concentration Adjustments	--	36,772	10
RWA after diversification	317,844	405,200	110

	Tier 1 capital	Tier 1 ratio (%)	Total adjusted capital	S&P Global RAC ratio (%)
Capital ratio				
Capital ratio before adjustments	35,190	**11.1**	33,501	**9.1**
Capital ratio after adjustments‡	35,190	**11.1**	33,501	**8.3**

*Note: S&P Global Ratings-calculated. With the revision in the BICRA group of Israel to '3' from '4', reflecting our view of the supportive domestic environments, the risk weights that are being applied to the exposures in RAC are lower, leading to a RAC above 10% in the next couple of years. *Exposure at default. §Securitization Exposure includes the securitization tranches deducted from capital in the regulatory framework. †Exposure and S&P Global Ratings' risk-weighted assets for equity in the banking book include minority equity holdings in financial institutions. ‡Adjustments to Tier 1 ratio are additional regulatory requirements (e.g. transitional floor or Pillar 2 add-ons). RWA--Risk-weighted assets. RW--Risk weight. RAC--Risk-adjusted capital. ILS--New Israeli Shekel. Sources: Company data as of Dec. 31, 2017, S&P Global.

Risk profile: risks adequately covered by capital buffer

In our opinion, Bank Leumi's risk profile is similar to that of other large Israeli banks. Compared with other larger and more diversified peers operating in other countries with a similar economic risk, and despite sound asset quality indicators, we consider the Bank's risk exposure as more concentrated. This reflects geographical focus in Israel and the relatively concentrated nature of the domestic economy. Given the high concentration in the commercial real estate and mortgage lending in the Bank's overall business mix (47% in the first half of 2019), adverse developments in those sectors might expose the Bank to risks. Nevertheless, the Bank continues its efforts to mitigate the risk and diversify the credit risks by reducing exposure to single borrowers and leveraged lending.

We predict credit growth to remain moderate in 2019-2020, although slightly higher than recently. Although no longer constrained by the need to increase the Bank's capital, book growth will also be constrained by new dividend policy and the capital management measures.

Although Bank Leumi and its domestic peers have a high exposure to real estate lending, we now consider this risk to be more limited as a consequence of the stabilization of prices in the last couple of years, and the macroprudential measures taken by the regulator. Our base scenario does not predict a sharp correction in house prices, but rather a more moderate increase in prices compared with the last decade given the government's initiatives designed to increase the supply in the housing market. Measures taken by the Bank of Israel also help mitigate the risks inherent in large mortgage exposures, since the loan to value (LTV) rates in Israel are very low compared to other developed countries. Macroprudential measures also include payment-to-income tests and cap the amounts of floating rate debt a borrower may take.

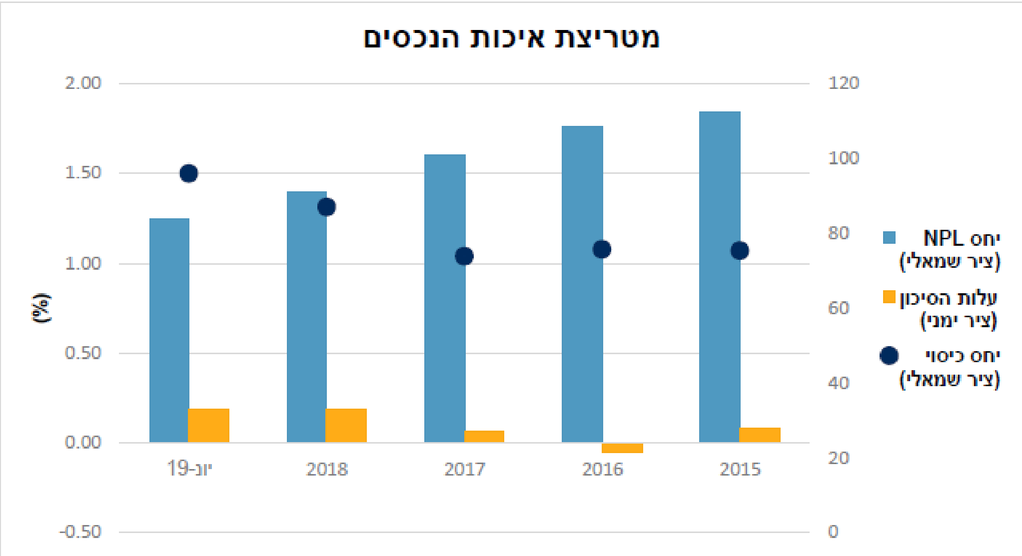
As of June 30 2019, the Bank's lending to the construction and commercial real estate sectors accounts for 16% of the Bank's loan portfolio, although the construction loans are mainly residential loans. The commercial real estate sector seems relatively robust, supported by rising demand to office spaces from the services industry and the continual increase in private consumption. At the same time, the low interest rates support the financial position of the commercial real estate companies. On the other hand, rapid growth in office space in 2018, after a 16-year record high of completions, might, in our opinion, cerate oversupply in the next few years. Moreover, shopping malls might suffer as a result of the growth in e-commerce which has an adverse effect on retailers, and we believe that in several cities in Israel there is an oversupply of commercial spaces.

Recently, the Bank adopted a more cautious approach toward consumer credit, a traditional growth engine in recent years in the industry as a whole. We believe that the risk involved in this type of credit is higher, which is reflected in higher interest margins and leads to larger provisions for credit losses. The recently adopted insolvency law could in particular hinder the collection process, and strong consumer lending growth from non-bank entities may have an adverse effect on the quality of retail credit. We consider that the still relatively low household leverage relative to GDP and the bank's recent tightening of underwriting and slowdown in lending in this segment is significantly mitigating credit risks. We also highlight that Leumi's retail lending is more heavily weighted to mortgages and its recent loss experience in consumer and small business credit has been lower than industry averages.

Given the small size of Israel's economy, Bank Leumi's position as one of the country's two largest corporate lenders means that single-name-borrower concentrations also represent a source of incremental risk, compared with banks in larger countries with more diverse economies. However, Leumi has traditionally had a strong middle market presence where risks are more diversified. The gradual dismantling of domestic holding company structures coupled with active market for risk-transfer to institutional investors and the bond market, is also allowing the Bank flexibility in managing its corporate exposures.

Nonperforming assets at Leumi continued to decrease, amounting to 1.24% of total loans as of the first half of 2019, which we consider very good in a global comparison and adequate compared with local peers. Although we expect the economic environment in Israel will remain broadly supportive, we don't forecast asset quality will improve further over the next few years. We believe the cost of risk bottomed out last year, after reaching unsustainably low levels due to sufficient recoveries in the corporate segment. We expect loan loss provisions will increase somewhat in the next couple of years, to about 30 base points from about 20 base points in first-half 2019, but will remain contained overall. Nevertheless, our estimate of losses does not include the impact of the upcoming adoption of the current expected credit losses (CECL) accounting standard on Jan.1, 2022. We understand that banks will have a preparation phase, so the impact on provisions, reported nonperforming loans (NPLs), and regulatory capital ratios will only become clear during the run-up to, and final implementation of, CECL. We consider the bank's coverage ratio of nonperforming loans and 90 day past due loans of 96% on June 30 2019, to be broadly in line with global standards.

Chart 5



Source: S&P Global Ratings

A key non-credit risk for the Bank is the volatility in the actuarial valuation of its pension schemes offered to employees until the end of 1999. Previously, the fund's size and the decline in discount rates have acted as a drag on the bank's capital building. However, given current low interest rates, the valuation adjustment would be positive for capital building should rates increase.

Operational risks are material, but not bank-specific. They mainly relate to the geopolitical tensions in the region and potential damage to the bank in case of tail events. We reflect these risks in our anchor BICRA assessment. In our view, Leumi is adequately protecting itself from cyber risks.

Table 5.

Bank Leumi Le-Israel B.M. Risk Position (%)

	YTD June 2019	2018	2017	2016	2015
Growth in customer loans	4.3	1.3	2.2	0.2	3.3
Total managed assets/adjusted common equity (x)	13.7	13.8	14.9	15.0	14.9
New loan loss provisions/average customer loans	0.2	0.2	0.1	(0.0)	0.1
Net charge-offs/average customer loans	0.2	0.1	0.1	0.0	0.2
Gross nonperforming assets/customer loans + other real estate owned	1.2	1.4	1.6	1.8	1.8
Loan loss reserves/gross nonperforming assets	96.0	87.0	73.8	75.7	75.3

Data are based on S&P Global Ratings adjusted number and ratios.

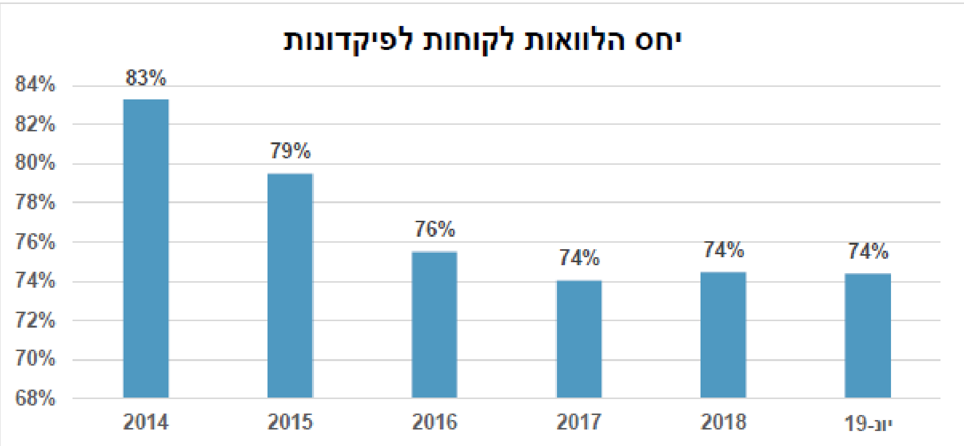
Funding and liquidity: Sound liquidity supported by extensive domestic funding base and good liquidity indicators

We assess Leumi's funding as average and its liquidity as adequate. As of the first half of 2019, customer deposits were fully funding loans, with the ratio of total loans to customer deposits at 74%, which we think is not out of line with broad industry average also better than some peers.

During the first half of 2019, Leumi's stable funding ratio was 132%, close to the local industry average. We believe the funding profile, both at the bank and industry wide, are sound. We regard this as a strength for our overall banking industry assessment (BICRA) for Israel and reflect this in the anchor assessment.

Leumi benefits from sound liquidity, supported by its extensive domestic funding base, which is highly diverse and dominated by retail deposits with moderate deposit-pricing competition.

Chart 6

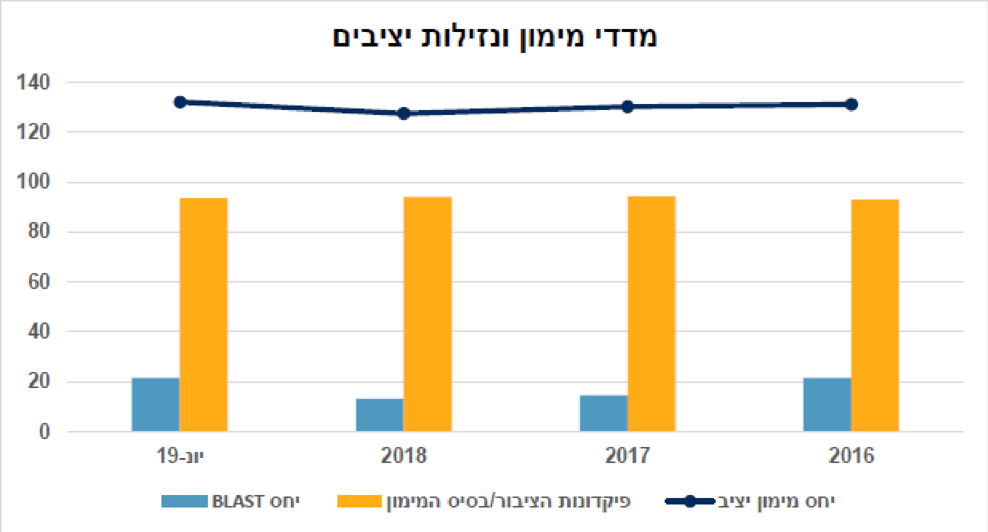


Source: S&P Global Ratings

The Bank’s liquid asset cushions are material, with cash, central bank, and other bank placements, and investment securities (two-thirds of which consist of Israeli and foreign governments bonds) constituting one-third of assets on June 30, 2019. Bank Leumi is a net placer of funds on the interbank market.

Apart from its deposit funding base, the Bank has recourse to wholesale funding, issuing bonds, subordinated notes, and hybrid instruments in the domestic market. As of the first half of 2019, debt issues outstanding constituted 6%of total funding. The Bank’s ratio of broad liquid assets to short-term wholesale funding was 22x as of June 30 2019, indicating its low reliance on such wholesale funding.

Chart 7



Source: S&P Global Ratings

Table 6.

Bank Leumi Le-Israel B.M. Funding and Liquidity (%)

	YTD June 2019	2018	2017	2016	2015
Core deposits/funding base	93.5	93.9	94.5	92.9	92.7
Customer loans (net)/customer deposits	74.4	74.4	74.0	75.5	79.5
Long term funding ratio	98.6	97.8	97.9	98.6	98.3
Stable funding ratio	132.1	127.4	130.2	131.1	124.4
Short-term wholesale funding/funding base	1.5	2.4	2.3	1.5	1.8
Broad liquid assets/short-term wholesale funding (x)	21.6	13.1	14.5	21.7	15.8
Net broad liquid assets/short-term customer deposits	42.0	38.5	40.9	42.2	36.1
Short-term wholesale funding/total wholesale funding	23.4	39.6	41.2	21.3	24.6

Data are based on S&P Global Ratings adjusted number and ratios.

External support: Potential government support

The Bank’s Issuer Credit Rating (ICR) is one notch higher than its Stand-Alone Credit Profile (SACP), reflecting its high systematic importance in Israel and the government’s ‘supportive’ policy toward the domestic banking sector. In our view, there is a moderately high likelihood that the government would provide extraordinary support to the Bank if necessary. We believe both the government and the central bank acknowledge the importance of a stable banking sector. In our opinion, the central bank has adequate capacity to support the industry's funding and capital needs.

Additional rating factors

The sale of Leumi Card was completed in February 2019, so as from June 2019 it does not appear in the Bank's balance sheet. However, the gain on sale is recorded in the income statement as a non-interest income. In the June 2019 report, prior period statements have excluded Leumi Cards data for comparative analysis, labelled as "Pro Forma Information Excluding Leumi Card."

Methodology and related articles

- Methodology – General: Use Of CreditWatch And Outlooks, September 14, 2009
- Methodology: Bank Rating Methodology: November 9, 2011
- Methodology: Banking Sector Risk Assessment Methodology, November 9, 2011
- Methodology: Quantitative Metrics for Rating Banks Globally: July 17, 2013
- Methodology: Timelines of Payments: Grace Periods, Guarantees, And Use of 'D' (Default) and 'SD' (Selective Default) Ratings: October 24, 2013
- Methodology: Methodology For Linking Long-Term And Short-Term Ratings: April 7, 2017
- Methodology: Methodology For Assessing the Risk-Adjusted Capital of Financial Institutions: July 20, 2017
- Methodology – General: National and Regional Scale Credit Ratings: June 25, 2018
- Methodology – General: Rating of Hybrid Capital, July 1 2019
- Methodology – General: Rating of Group Companies, July 1 2019
- S&P Global Ratings Definitions: July 5 2019
- Opinions and interpretation: The Relationship Between the Global Rating Scale and the Israeli Rating Scale: June 26, 2018

General details (as of November 7, 2019)

Bank Leumi of Israel Ltd.	
Issuer's Rating(s)	
Long term	ilAAA\Stable
Issuance's Rating(s)	
Hybrid subordinated debt	
Subordinated bonds with loss absorption mechanism Series 400, 401, 402, 403	ilAA
Leumi subordinated capital notes Series 200, 201	ilAA
Series 404	ilAA
Subordinated capital notes Series 300, 301	ilAA
Unsecured senior debt	
Bonds – Series 177, 178, 179	ilAAA
Bonds – Series 180	ilAAA
Subordinated debt	
Subordinated bonds Series N	ilAA+
Issuer's Rating History	
Long term	
October 07, 2014	ilAAA\Stable
May 5, 2010	ilAA+\Stable
April 30, 2009	ilAA+\Negative
June 21, 2007	ilAAA\Stable
May 14, 2006	ilAAA
February 1, 2003	ilAA+
May 1, 1998	ilAAA
Additional details	
Date and time on which the event took place	07/11/2019 14:18
Date and time on which the event first became known	07/11/2019 14:18
Entity that initiated the rating	The rating company

Credit rating monitoring

We monitor developments that may impact the credit rating of issuers or specific bond series rated by us on an ongoing basis. The purpose of monitoring is to ensure that the rating will be up-to-date on a current basis and to identify the parameters that may trigger a change in rating.

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