CREDIT OPINION
8 October 2024

Update

Send Your Feedback

RATINGS

Israel Discount Bank Ltd.

Domicile	Tel Aviv, Israel
Long Term CRR	Baa1
Type	LT Counterparty Risk Rating - Fgn Curr
Outlook	Not Assigned
Long Term Debt	Baa1
Type	Senior Unsecured - Fgn Curr
Outlook	Negative
Long Term Deposit	Baa1
Type	LT Bank Deposits - Fgn Curr
Outlook	Negative

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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Israel Discount Bank Ltd.

Update following ratings downgrade

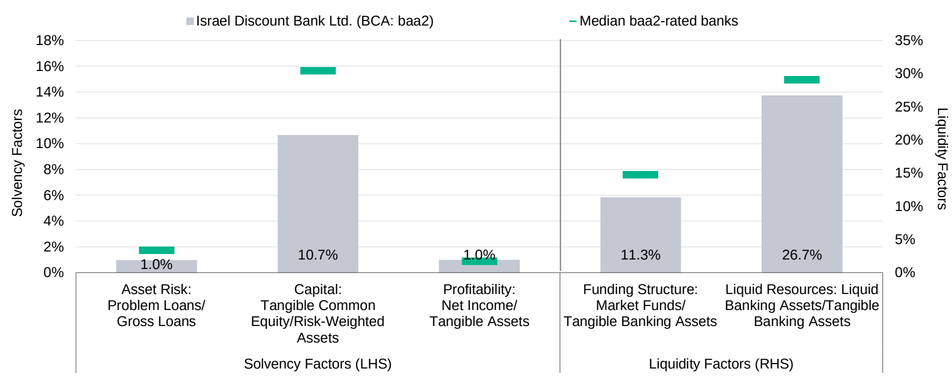
Summary

Israel Discount Bank Ltd. (IDB)'s Baa1 long-term deposit ratings reflect (1) the bank's baa2 Baseline Credit Assessment (BCA); and (2) one notch of rating uplift based on our assessment of a very high probability of support from the Government of Israel (Baa1 negative), in case of need.

IDB's baa2 BCA reflects its deposit based funding structure along with comfortable liquidity, currently low problem loans and strengthened recurring profitability supported by efficiency gains and robust business growth potential.

High geopolitical risks are captured in the BCA and the negative rating outlook. IDB's standalone BCA also reflects relatively modest but stable capital buffers, which are below similarly-rated international peers mainly reflecting Bank of Israel's (BoI) conservative risk-weighting and additional downside risks from a significant exposure concentration to the property market.

Exhibit 1
Rating Scorecard - Key financial ratios



These are our Banks Methodology scorecard ratios. Asset Risk and Profitability reflect the weaker of either the latest figure or the three-year and latest figure average. Capital is the latest reported figure. Funding Structure and Liquid Resources reflect the latest fiscal year-end figures.
Source: Moody's Ratings

Credit strengths

» Stable deposit-based funding structure and comfortable liquidity

» Asset quality has been strong

» Strengthened ongoing profitability, supported by enhanced efficiency

» Very high likelihood of government support, in case of need

Credit challenges

» Geopolitical risks have increased and asset quality will likely deteriorate because of the impact of the military conflict

» Exposure concentration in real estate is also a downside risk

» Modest risk-weighted capitalisation, but moderate leverage

» Operating cost base remains higher relative to peers

Outlook

The negative outlook on the bank's long-term deposit ratings captures both the negative outlook on the Government of Israel's rating and therefore the potential further weakening of the sovereign's capacity to provide support, together with the risk that the bank's standalone fundamentals may be more severely and sustainably affected because of weaker economic growth and investment climate, and a more adverse impact from the conflict on key sectors and individual borrowers.

Factors that could lead to an upgrade

» There is a limited scope for an upgrade of the bank's deposit ratings given the negative outlook. We could stabilise the outlook on the bank's ratings in case the outlook on the sovereign rating changes to stable and/or downside risks to the economy and the bank subside.

Factors that could lead to a downgrade

» The bank's long-term deposit ratings could be downgraded if the sovereign rating is downgraded further, or if the banks' own standalone BCAs are downgraded by more than one notch.

» The banks' BCAs could be downgraded in case of a severe escalation of the conflict and/or an adverse and long-term impact on the economy, and therefore a sustained or significant impact on their standalone fundamentals, or if any individual bank's performance proves more volatile than in previous conflicts and economic crises.

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the issuer/deal page on https://ratings.moodys.com for the most updated credit rating action information and rating history.

Key indicators

Exhibit 2
Israel Discount Bank Ltd. (Consolidated Financials) [1]

	06-24[2]	12-23[2]	12-22[2]	12-21[2]	12-20[2]	CAGR/Avg.[3]
Total Assets (ILS Million)	401,292.0	395,724.0	376,754.0	335,088.0	293,969.0	9.3[4]
Total Assets (USD Million)	106,522.6	109,895.9	106,774.6	107,913.6	91,556.3	4.4[4]
Tangible Common Equity (ILS Million)	31,405.0	29,413.0	26,051.0	21,068.0	18,189.3	16.9[4]
Tangible Common Equity (USD Million)	8,336.4	8,168.2	7,383.0	6,784.9	5,665.0	11.7[4]
Problem Loans / Gross Loans (%)	0.9	0.9	0.7	1.4	1.9	1.2[5]
Tangible Common Equity / Risk Weighted Assets (%)	10.7	10.7	10.3	9.6	9.1	10.1[6]
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	6.7	7.4	5.6	13.1	17.2	10.0[5]
Net Interest Margin (%)	2.8	2.9	2.5	2.1	2.1	2.5[5]
PPI / Average RWA (%)	2.7	3.1	2.5	1.9	1.9	2.4[6]
Net Income / Tangible Assets (%)	1.1	1.1	0.9	0.9	0.5	0.9[5]
Cost / Income Ratio (%)	50.9	48.5	54.7	62.8	61.7	55.7[5]
Market Funds / Tangible Banking Assets (%)	10.4	11.3	9.6	8.0	8.5	9.6[5]
Liquid Banking Assets / Tangible Banking Assets (%)	25.5	26.7	28.2	30.3	29.1	28.0[5]
Gross Loans / Due to Customers (%)	90.8	89.4	84.4	83.8	86.5	87.0[5]

[1] All figures and ratios are adjusted using Moody's standard adjustments. [2] Basel III - fully loaded or transitional phase-in; LOCAL GAAP. [3] May include rounding differences because of the scale of reported amounts. [4] Compound annual growth rate (%) based on the periods for the latest accounting regime. [5] Simple average of periods for the latest accounting regime. [6] Simple average of Basel III periods.
Sources: Moody's Ratings and company filings

Profile

IDB is the fourth-largest banking group in Israel by assets with a 16% market share and total consolidated assets of NIS401 billion (around $107 billion) as of June 2024. IDB also had a 15% market share in deposits and 17% in loans as of the same date.

Domestically, IDB provides a full range of banking services out of its 173 branches in Israel as of June 2024. IDB has the largest international operations among Israeli banks, mainly carried out through Israel Discount Bank of New York (IDB New York), its US subsidiary, which focuses on mid-sized companies and private banking. IDB New York operates branches in New York, Florida and California and has representative offices in Latin America and in Israel.

The bank's other key subsidiaries include Mercantile Discount Bank, a niche bank specialising in retail, small and medium-sized and municipal banking, and Israel Credit Cards (ICC), its 71.8% owned credit card company.

IDB is currently the only Israeli bank to consolidate a credit card company, after the two-largest Israeli banks were required to divest their own credit card units. A decision by the Minister of Finance was taken in January 2023 that effectively requires IDB to divest of its controlling stake in ICC. ICC's contribution to IDB's consolidated net profit for 2023 amounted to around 5%.

IDB was incorporated in 1935. The bank's common stock trades on the Tel Aviv Stock Exchange (ticker: DSCT).

Source of facts and figures cited in this report

Unless noted otherwise, we have sourced data relating to systemwide trends and market shares from the central bank. Bank-specific figures originate from the banks' reports and are based on our own chart of accounts and may be adjusted for analytical purposes. Please refer to Financial Statement Adjustments in the Analysis of Financial Institutions published on 8 April 2024. We do not use the Bank of Israel's exchange rates in converting figures from Israeli shekel into US dollars, so US dollar figures may differ from bank reported figures.

Detailed credit considerations

Strong asset quality that will likely deteriorate

IDB's asset quality will deteriorate from strong levels because of the damage to Israel's economy caused by the military conflict that has already lasted longer than most of its previous conflicts. The bank has provisioned against downside scenarios. In addition to risks from geopolitical tensions and similarly to other Israeli banks, the bank's exposure concentration to Israel's real estate market is also a downside risk for its asset quality.

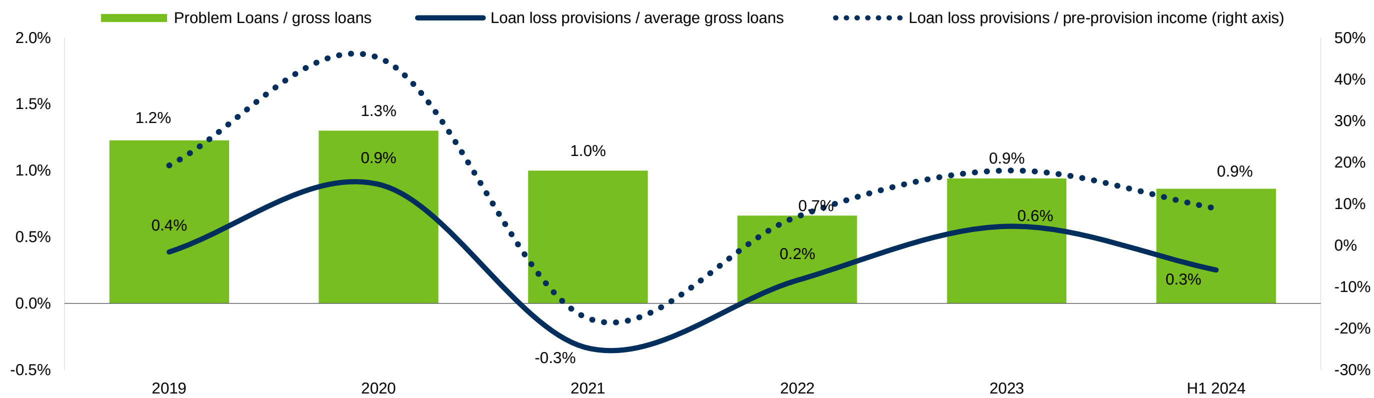
The bank's higher than peer-average loan growth in recent years (loans grew by a compound annual rate of 10% over the period 2017-2023, although growth moderated to 8% in 2023 and 4% in the first six months of 2024) that drives some unseasoned risk and its previous through-the-cycle performance that had been somewhat weaker than its peers are also reflected in our assessment, along with a recent structural reduction in portfolio asset risk. IDB's average cost of risk in the period 2006-2019 (before the pandemic) was 0.47%, reflecting a lower historical proportion of housing loans. Once IDB no longer consolidates a credit card company, its credits costs will likely be lower and further aligned with the domestic peer average.

IDB's problem loans (defined as non-accruing loans and accruing loans that are more than 90 days overdue) to gross loans were a low 0.9% as of June 2024 (see Exhibit 3). In 2023, credit costs (loan loss provision expenses to average gross loans) increased to 0.6% mainly driven by group provisions booked in the last two quarters of 2023 against the potential impact of the conflict on borrowers. Credit costs were lower at 0.3% in the first six months of 2024, mainly reflecting collective provisions.

Exhibit 3

IDB's asset quality has been strong, with a low level of problem loans and contained credit losses in recent years

Evolution of problem loans and credit costs



For 2020 and 2021, problem loans were adjusted in this chart to remove a predominantly government-backed exposure that was more than 90 days overdue

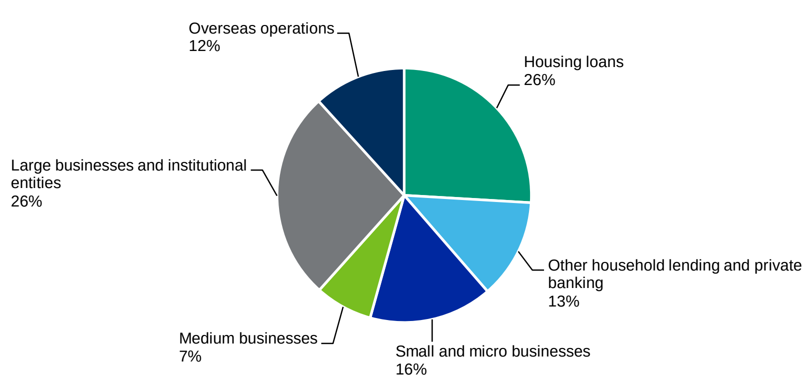
Sources: Bank's financial statements; Moody's Ratings

Asset risk in IDB's loan portfolio had been reducing, reflecting an increasing share of relatively lower-risk residential mortgages that are a key strategic focus for the bank and accounted for 26% of the bank's loan book as of June 2024 (see Exhibit 4), compared to 20% at end-2018. Also, in recent years, the bank tightened its credit standards both in retail and business lending, eliminated exposures to holding companies and reduced borrower concentrations.

Exhibit 4

IDB's loan book is fairly diversified by customer type

Loan book breakdown as of June 2024 (supervisory operating segments)



Source: Bank's financial results

Sector concentration to real estate is high, which exposes the bank to the risk of a sustained disruption in activity in the sector, as well as the risk of a sharp property price correction together with reduced ability of borrowers to service their loans. Beyond mortgages, lending to the construction and real estate sector made up 16% of IDB's gross loans as of June 2024. Although lower than its larger peers, the bank's exposure grew by a still high 9% year-over-year as of June 2024. Residential projects where risk is mitigated by close oversight of closed residential construction made up 34% of total credit risk in the sector as of June 2024, while income generating properties were 24%.

Modest risk-weighted capitalisation, but moderate leverage

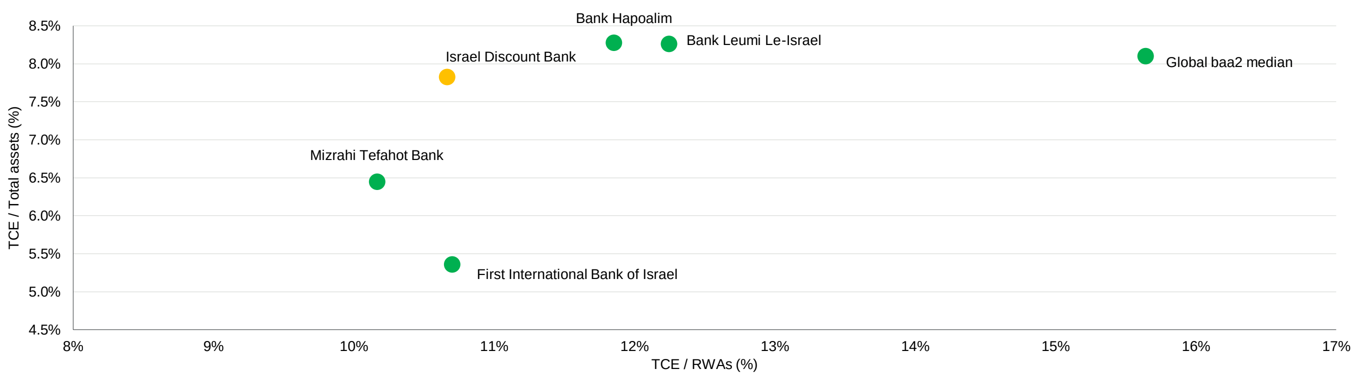
IDB's risk-weighted capitalisation is modest. But, although such metrics are below global peers, the bank's loss-absorption buffers are supported by conservative regulatory risk-weights that result in higher loss-absorption buffers and drive stronger leverage. For example, mortgages are risk-weighted according to their loan-to-value and have an average risk weight of over 50% in Israel, which is higher than the 35% risk weight normally used in the standardised approach. The bank's capital ratios are also more stable compared to banks globally that use a model based approach in calculating credit risk-weighted assets (RWAs).

IDB's tangible common equity (TCE)/RWAs capital ratio was 10.7% as of June 2024, below the global median (see Exhibit 5). The bank's Basel III leverage ratio was 6.9% as of June 2024, above the 4.5% minimum regulatory requirement that applied at that time. Its TCE-to-total assets ratio was 7.8% as of the same period.

Exhibit 5

IDB's risk-weighted capitalisation is lower than global peers driven by conservative risk weights

Risk-weighted capitalisation and leverage of Israeli banks and the global median



Source: Moody's Ratings

IDB also reported a Common Equity Tier 1 (CET1) ratio of 10.7% as of June 2024, the highest level in recent years and up from 10.3% as of end-2022. This substantially exceeded the 9.2% minimum regulatory requirement and the bank's own internal minimum threshold of 9.75%. Similarly to other periods of high volatility and in line with the BoI's guidance, IDB distributed earnings below its dividend distribution policy of up to 40% of net profits in each of the last four quarters.

Although the downgrade of Israel's sovereign rating will increase the risk-weights we use in our capital ratio to 50% and lower it by around 20 basis points in Q3 2024, provided high profitability continues and together with muted credit growth we expect capital levels to continue to rise overall. We expect them to gradually decline back to historical levels once uncertainty subsides.

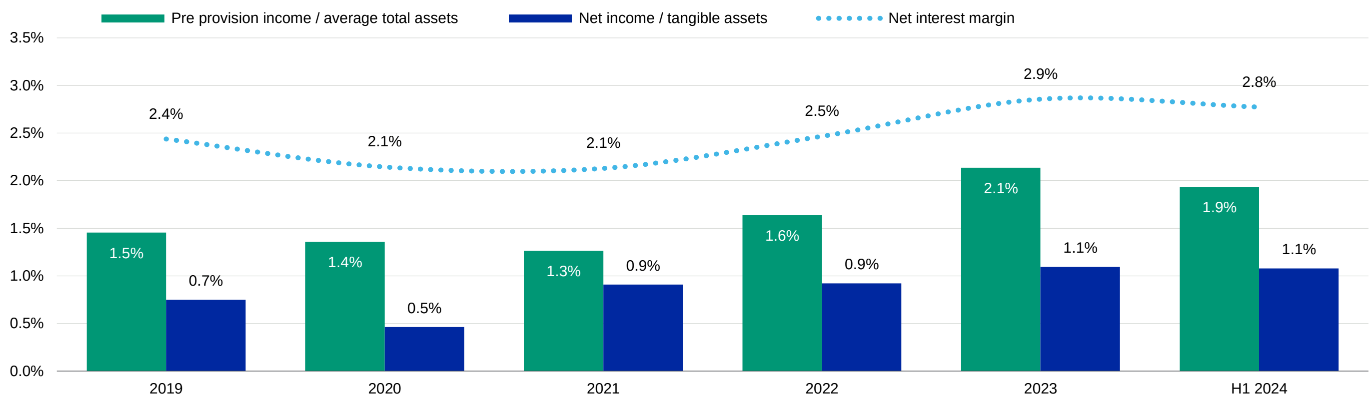
Through adjustments in earnings distributions, capital raising and RWAs management, IDB has demonstrated its ability to maintain steady capital ratios over time.

Strengthened ongoing profitability, which will decline from recent high levels

IDB's recurring profitability is moderate and has consistently improved in recent years, closing the gap with its domestic peers. Profitability benefitted from several cost initiatives and faster business growth than the rest of the banking system. Revenue growth alongside cost control have led to efficiency gains that support sustainable profitability strengthening internal capital generation, resiliency at times of stress and the bank's ability to resist growing competition. Operating costs declined to 2.0% of assets in the first six months of 2024, from over 2.5% before 2018, and the bank's reported cost-to-income ratio was 52%. However, IDB's cost base remains higher than its domestic peers, partly because it still consolidates a credit card company.

IDB reported net income equivalent to 1.1% of tangible assets in the first six months of 2024 and full-year 2023 (see Exhibit 6), up from an average of 0.7% between 2017 and 2019, because of higher interest rates, high CPI, as well as one-off items[1]. In the coming quarters, profitability will decline from recent exceptionally high levels because of subdued credit growth, higher bank taxes for 2024 and 2025 and potentially increased provisions in case macroeconomic expectations deteriorate. Still overall high interest rates, with the BoI's research department expecting that the policy rate will be 4.25% in the first quarter of 2025 compared to 4.5% currently, will be supportive of a healthy net interest margin and robust revenues.

Exhibit 6
IDB's profitability is moderate, having steadily improved in recent years



2022 and 2023 profits benefited from exceptional items, such as the sale of properties
Source: Moody's Ratings

The bank's net interest margin slightly narrowed to 2.8% in the first six months of 2024, from 2.9% in 2023, driven by the customer shift to higher-yielding deposit accounts, with the bank's non-interest bearing deposits accounting for 23% of total deposits as of June 2024 compared to 29% at end-2022. Margins are still higher, however, than the 2021 level because rate hikes allowed the bank to unlock the value from its low-cost core deposit base.

Stable deposit-based funding structure and comfortable liquidity

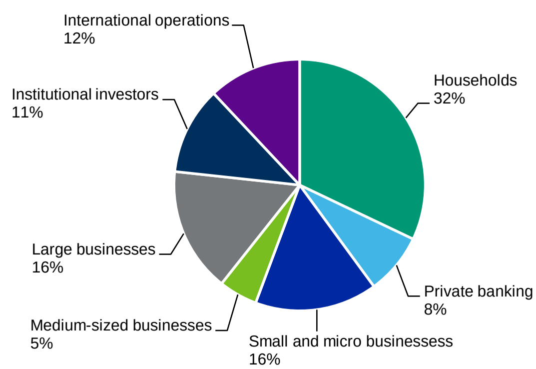
IDB's credit profile benefits from a stable domestic deposit-based funding structure, benefitting from the strong savings culture in Israel, and with limited reliance on more confidence-sensitive market funding. Customer deposits comfortably fund the bank's loan portfolio with a net loans-to-deposits ratio of 89% as of June 2024. Furthermore, market funds accounted for a low 10% of tangible banking assets as of the same date[2]. The bank had around NIS18 billion (5% of total assets) of bonds and subordinated notes outstanding as of June 2024. These balances were mainly sourced from the local capital market and allow for better matching of the bank's assets and liabilities maturities.

Granular household (excluding private banking) and small business deposits accounted for 48% of total deposits as of June 2024 (see Exhibit 7). Our assessment also considers that foreign deposits, which could be more vulnerable to an institution-specific loss in depositor confidence, made up 12% of total deposits as of June 2024. Nevertheless, deposits from institutional investors were 11% of total deposits, considerably lower than peers. We note that both domestic and foreign deposits had remained stable during past systemic shocks in Israel.

Exhibit 7

Granular retail deposits make up a large part of IDB's deposit base

Breakdown of deposits by segment as of June 2024



Source: Bank's financial statements

The bank maintains comfortable liquidity buffers at 26% of tangible banking assets as of June 2024. Cash and interbank balances accounted for 12% of assets, with securities accounting for an additional 14%. The securities portfolio primarily comprises Israeli government securities at 68% of total, and to a lesser extent mortgage-backed and asset-backed securities of US government agencies (15% of total), while 4% of the securities portfolio were investments in shares. IDB reported a liquidity coverage ratio at 133% and a net stable funding ratio of 121% as of June 2024, significantly above the respective 100% minimum requirement.

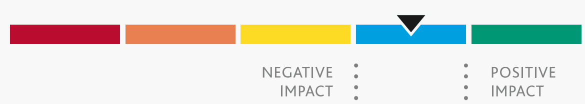
ESG considerations

Israel Discount Bank Ltd.'s ESG credit impact score is CIS-2

Exhibit 8

ESG credit impact score

CIS-2



ESG considerations do not have a material impact on the current rating.

Source: Moody's Ratings

IDB's **CIS-2** indicates that ESG factors are not material to the current ratings because a high level of government support mitigates the impact from ESG risks, which have lately increased (especially social risks) because of the military conflict and the high customer relations risks in Israel.

Exhibit 9

ESG issuer profile scores

Source: Moody's Ratings

Environmental

IDB faces moderate exposure to environmental risks, mainly because of its portfolio exposure to carbon transition risks as a diversified bank and one of Israel's five largest banks with a significant corporate exposure. In line with its peers, IDB faces growing business risks and stakeholder pressure to meet broader carbon transition goals. IDB is engaging in further developing its climate risk and relevant portfolio management capabilities and increasing its green financing.

Social

IDB faces high social risks, related to societal and demographic trends as well as from customer relations. The current military conflict may cause a severe disruption of the economy and impact the bank's financial performance, depending on its duration and scale. However, a relatively young and growing population in Israel affords business opportunities for the bank. Further, IDB faces high customer relations risk because of the considerable focus on consumer protection in Israel, exposing banks to potential fines from regulators and litigation from customers. High cyber and personal data risks are mitigated by a sound IT framework.

Governance

IDB faces overall low governance risks. The bank's financial strategy is transparent and conservative, under the oversight of a proactive and hands-on regulator, and its risk management is in line with industry practices and commensurate with its universal banking model. The bank also provides timely and detailed external reporting. However, the bank's US subsidiary is under increased scrutiny and has entered into consent orders with its US regulators to address identified compliance shortcomings and to enhance its policies, procedures, controls and staffing levels. The orders include a look-back review of past transactions. We will monitor the outcome of this process and any risks that may emerge.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moodys.com. In order to view the latest scores, please click here to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

Support and structural considerations

Government support considerations

IDB's Baa1 deposit ratings incorporate one notch of government support uplift from the bank's baa2 Adjusted BCA because of our expectation of a very high probability of extraordinary support from the Israeli authorities. This assessment is based on IDB's systemic importance as one of the country's five-largest banking groups and the Israeli government's long standing practice of supporting systemically important banks in case of need.

Methodology and scorecard

About Moody's Bank Scorecard

Our Bank Scorecard is designed to capture, express and explain in summary form our Rating Committee's judgment. When read in conjunction with our research, a fulsome presentation of our judgment is expressed. As a result, the output of our Scorecard may materially differ from that suggested by raw data alone (though it has been calibrated to avoid the frequent need for strong divergence). The Scorecard output and the individual scores are discussed in rating committees and may be adjusted up or down to reflect conditions specific to each rated entity.

Rating methodology and scorecard factors

Exhibit 10
Rating Factors

Macro Factors		
Weighted Macro Profile	**Moderate +**	**100%**

Factor	Historic Ratio	Initial Score	Expected Trend	Assigned Score	Key driver #1	Key driver #2
Solvency						
Asset Risk						
Problem Loans / Gross Loans	1.0%	a2	↓↓	ba1	Sector concentration	Expected trend
Capital						
Tangible Common Equity / Risk Weighted Assets (Basel III - transitional phase-in)	10.7%	ba2	↔	ba1	Stress capital resilience	Nominal leverage
Profitability						
Net Income / Tangible Assets	1.0%	baa3	↔	ba1	Expected trend	
Combined Solvency Score		baa2		ba1		
Liquidity						
Funding Structure						
Market Funds / Tangible Banking Assets	11.3%	baa1	↔	baa2	Deposit quality	
Liquid Resources						
Liquid Banking Assets / Tangible Banking Assets	26.7%	baa2	↔	baa2	Expected trend	
Combined Liquidity Score		baa1		baa2		
Financial Profile				baa3		
Qualitative Adjustments				Adjustment		
Business Diversification				0		
Opacity and Complexity				0		
Corporate Behavior				0		
Total Qualitative Adjustments				0		
Sovereign or Affiliate constraint				Baa1		
BCA Scorecard-indicated Outcome - Range				baa2 - ba1		
Assigned BCA				baa2		
Affiliate Support notching				0		
Adjusted BCA				baa2		

Instrument Class	Loss Given Failure notching	Additional notching	Preliminary Rating Assessment	Government Support notching	Local Currency Rating	Foreign Currency Rating
Counterparty Risk Rating	1	0	baa1	-	Baa1	Baa1
Counterparty Risk Assessment	1	0	baa1 (cr)	-	Baa1(cr)	
Deposits	0	0	baa2	-	Baa1	Baa1
Senior unsecured bank debt	0	0	baa2	-		Baa1

[1] Where dashes are shown for a particular factor (or sub-factor), the score is based on non-public information.
Source: Moody's Ratings

Ratings

Exhibit 11

Category	Moody's Rating
ISRAEL DISCOUNT BANK LTD.	
Outlook	Negative
Counterparty Risk Rating	Baa1/P-2
Bank Deposits	Baa1/P-2
Baseline Credit Assessment	baa2
Adjusted Baseline Credit Assessment	baa2
Counterparty Risk Assessment	Baa1(cr)/P-2(cr)
Senior Unsecured	Baa1

Source: Moody's Ratings

Endnotes

1 These relate to profits from the sale of properties as part of the relocation of the bank's head offices and operations to a different central location.

2 Based on Moody's estimate for the bank's quarterly figures, given lack of breakdown between senior and subordinated debt. Subordinated debt is not included in Moody's definition of market funding.

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