

CREDIT OPINION

7 August 2024

Update

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RATINGS

Israel Discount Bank Ltd.

Domicile	Tel Aviv, Israel
Long Term CRR	A2
Type	LT Counterparty Risk Rating - Fgn Curr
Outlook	Not Assigned
Long Term Debt	A3
Type	Senior Unsecured - Fgn Curr
Outlook	Negative
Long Term Deposit	A3
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 to credit analysis

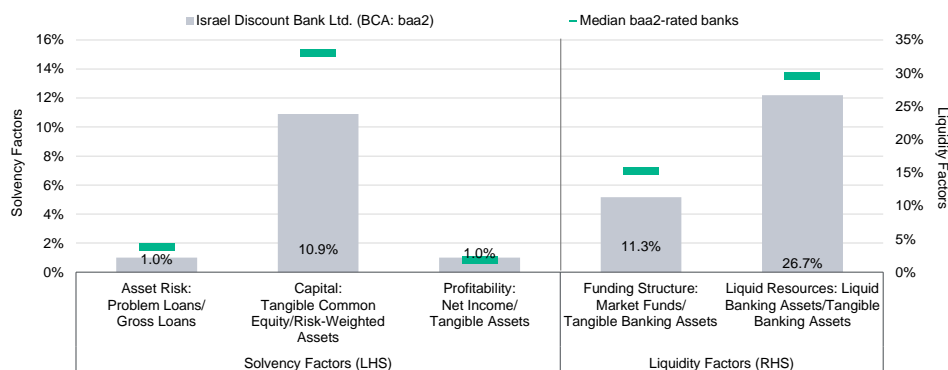
Summary

[Israel Discount Bank Ltd.](#) (IDB)'s A3 long-term deposit ratings reflect (1) the bank's baa2 Baseline Credit Assessment (BCA); and (2) two notches of rating uplift based on our assessment of a very high probability of support from the [Government of Israel](#) (A2 negative), in case of need.

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

Persistent 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

- » Given the crystallisation of geopolitical risks, asset quality will likely deteriorate
- » 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 long-term deposit ratings captures both the negative outlook on the Government of Israel's rating and the potential for a significantly more negative impact on the economy in the event of an escalation in the ongoing conflict, which could lead to the bank's standalone fundamentals being impacted more severely.

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's assets.

Factors that could lead to a downgrade

- » The deposit and senior unsecured debt ratings could be downgraded if both the sovereign rating and the standalone BCA are downgraded.
- » The bank's BCA could be downgraded in case of a prolonged and wider conflict that could have a significant impact on standalone fundamentals, or if the 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.moody's.com> for the most updated credit rating action information and rating history.

Key indicators

Exhibit 2

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

	03-24 ²	12-23 ²	12-22 ²	12-21 ²	12-20 ²	CAGR/Avg. ³
Total Assets (ILS Million)	390,097.0	395,724.0	376,754.0	335,088.0	293,969.0	9.1 ⁴
Total Assets (USD Million)	106,476.2	109,895.9	106,774.6	107,913.6	91,556.3	4.8 ⁴
Tangible Common Equity (ILS Million)	30,408.0	29,413.0	26,051.0	21,068.0	18,189.3	17.1 ⁴
Tangible Common Equity (USD Million)	8,299.8	8,168.2	7,383.0	6,784.9	5,665.0	12.5 ⁴
Problem Loans / Gross Loans (%)	0.9	0.9	0.7	1.4	1.9	1.2 ⁵
Tangible Common Equity / Risk Weighted Assets (%)	10.9	10.7	10.3	9.6	9.1	10.1 ⁶
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	7.0	7.4	5.6	13.1	17.2	10.1 ⁵
Net Interest Margin (%)	2.6	2.9	2.5	2.1	2.1	2.4 ⁵
PPI / Average RWA (%)	2.6	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 (%)	51.8	48.5	54.7	62.8	61.7	55.9 ⁵
Market Funds / Tangible Banking Assets (%)	9.9	11.3	9.6	8.0	8.5	9.5 ⁵
Liquid Banking Assets / Tangible Banking Assets (%)	25.1	26.7	28.2	30.3	29.1	27.9 ⁵
Gross Loans / Due to Customers (%)	91.0	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 NIS390 billion (around \$106 billion) as of March 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 March 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 1 February 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 impact of the ongoing military conflict. The bank has proactively 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.

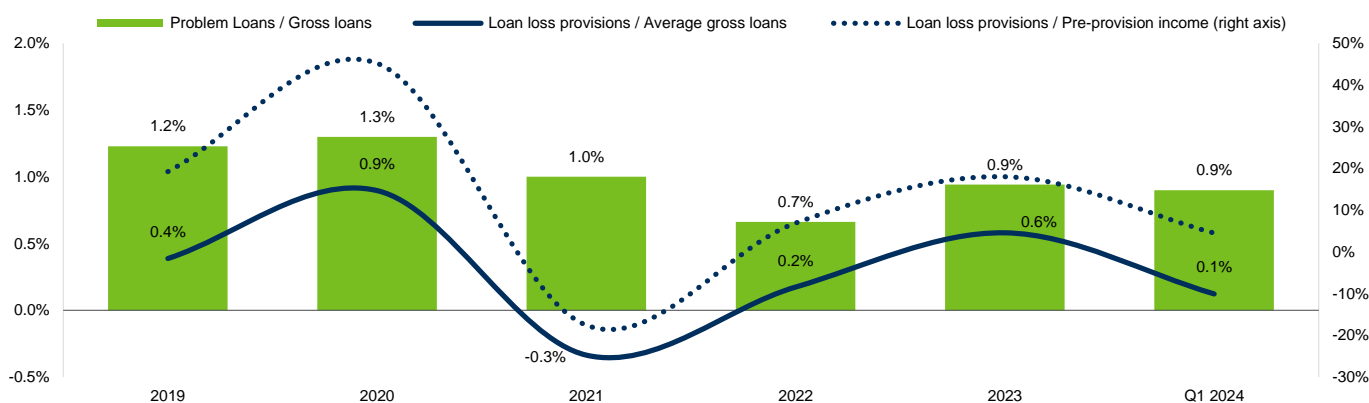
The bank's higher than peer-average loan growth in recent years (loans grew by a compound annual rate of 10% over the period 2017-2022, although growth moderated to 8% in 2023 and 1% in Q1 2024) that drives some unseasoned risk and its previous through-the-cycle performance that had been weaker than its peers are also reflected in our assessment, along with a recent structural reduction in 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 March 2024 (see Exhibit 3). Credit costs (loan loss provision expenses to average gross loans) were also low at 0.1% in the first three months of 2024. In 2023, credit costs increased to 0.6% mainly driven by group provisions booked in the last two quarters of 2023 against the potential impact of the war on borrowers.

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

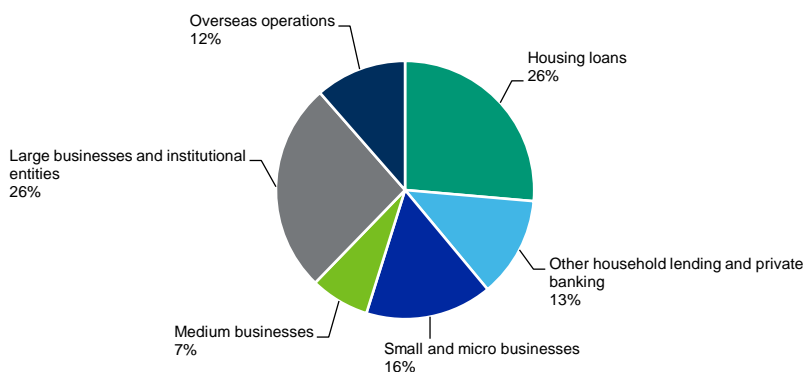
Sources: Bank's financial statements; Moody's Ratings

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 March 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 March 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 March 2024. Although lower than its larger peers, the bank's exposure grew by a still high 7% year-over-year as of March 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 March 2024, while income generating properties were 23%.

Modest risk-weighted capitalisation, but moderate leverage

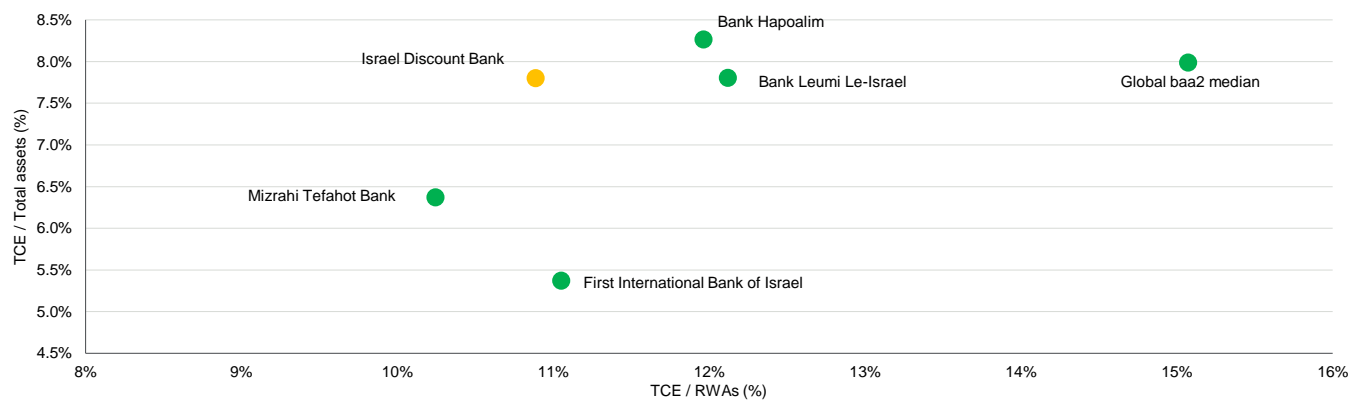
IDB's risk-weighted capitalisation is modest. But, although such metrics are below global peers, the bank's loss-absorption buffers are supported by conservative regulatory risk-weights that result in higher loss-absorption buffers and drive stronger leverage. For example, mortgages are risk-weighted 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 10.9% as of March 2024, below the global median (see Exhibit 5). The bank's Basel III leverage ratio was 6.9% as of March 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 10.9% as of March 2024, up from 10.3% as of end-2022 and substantially exceeding 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 two last quarters of 2023.

We expect capital levels to decline slightly once uncertainty subsides because of lower earnings retention. Through adjustments in earnings distributions, capital raising and RWAs management, IDB has demonstrated its ability to maintain steady capital ratios over time.

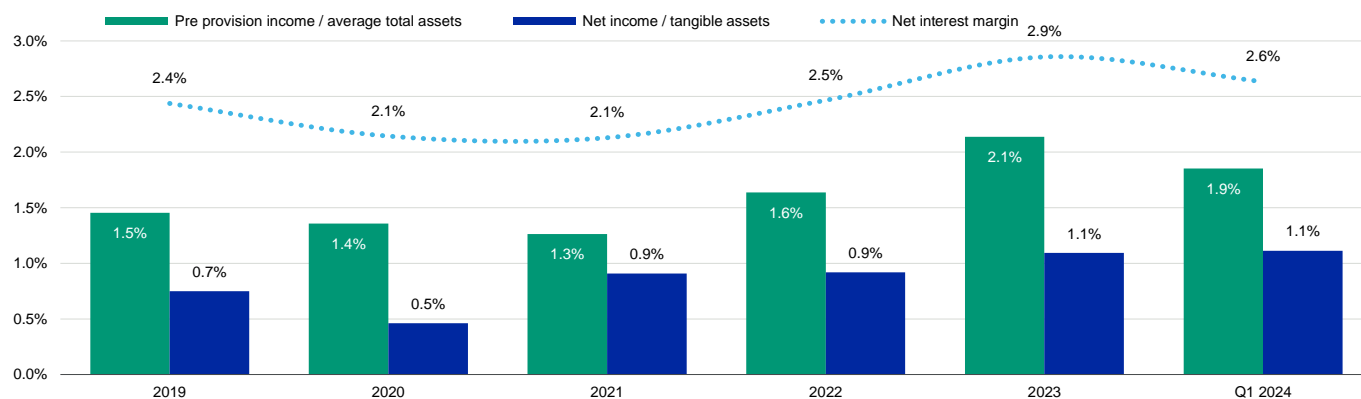
Strengthened ongoing profitability, which will decline from recent high levels

IDB's recurring profitability is moderate and has consistently improved in recent years, closing the gap with its domestic peers. Profitability benefitted from the 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 three months of 2024, from over 2.5% before 2018, and the bank's reported cost-to-income ratio was 53%. 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 three months of 2024 and full-year 2023, up from an average of 0.7% between 2017 and 2019 (see Exhibit 6), because of higher interest rates as well as one-off items¹. In the coming quarters, profitability will decline from recent exceptionally high levels because of subdued credit growth, support measures to customers affected by the conflict and higher bank taxes for 2024 and 2025. 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 narrowed to 2.6% in the first three months of 2024, from 2.9% in 2023, broadly at the same level as 2022, driven by the customer shift to higher-yielding deposit accounts, with the bank's non-interest bearing deposits accounting for 24% of total deposits as of March 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.

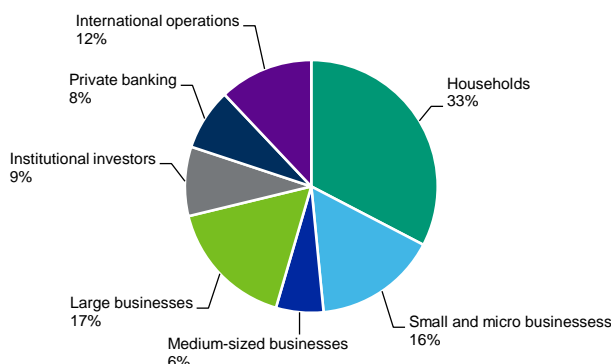
Stable deposit-based funding structure and comfortable liquidity

IDB's credit profile benefits from a stable funding structure that is driven by a domestic deposit base, 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 90% as of March 2024. Furthermore, market funds accounted for a low 10% of tangible banking assets as of the same date². The bank had around NIS18 billion (5% of total assets) of bonds and subordinated notes outstanding as of March 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 49% of total deposits as of March 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 March 2024. Nevertheless, deposits from institutional investors were 9% 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 March 2024



Figures do not add up to 100% due to rounding.
 Source: Bank's financial statements

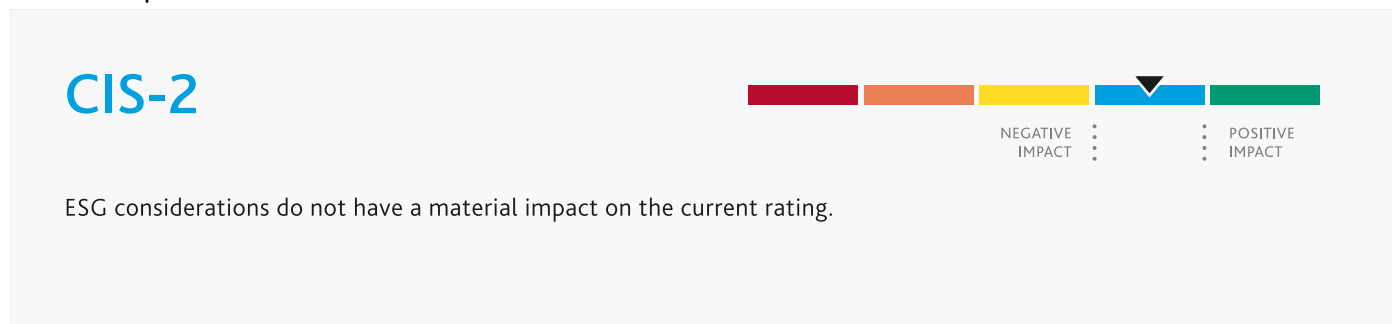
The bank maintains comfortable liquidity buffers at 25% of tangible banking assets as of March 2024. Cash and interbank balances accounted for 12% of assets, with securities accounting for an additional 14%. The securities portfolio primarily comprises Israeli government securities at 66% of total, and to a lesser extent mortgage-backed and asset-backed securities of US government agencies (17% of total), while 4% of the securities portfolio were investments in shares. IDB reported a solid liquidity coverage ratio at 142% and a net stable funding ratio of 123% as of March 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

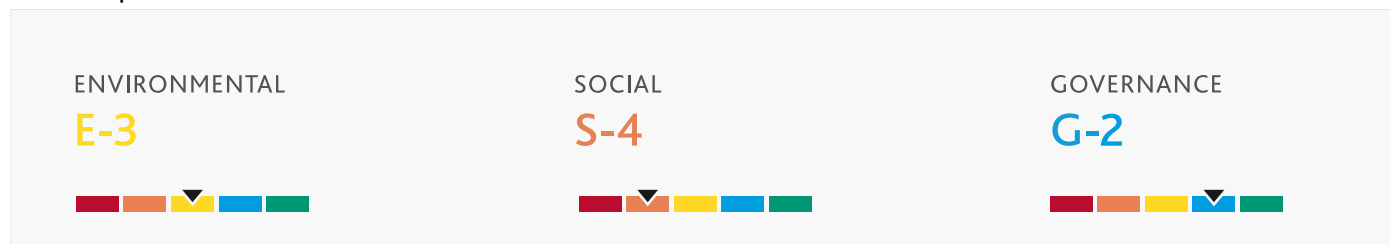


Source: Moody's Ratings

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 Moody's.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 A3 deposit ratings incorporate two notches 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	Strong -	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%	a1	↓↓	baa3	Sector concentration	Expected trend	
Capital							
Tangible Common Equity / Risk Weighted Assets (Basel III - transitional phase-in)	10.9%	ba1	↔	ba1	Risk-weighted capitalisation		
Profitability							
Net Income / Tangible Assets	1.0%	baa2	↓↓	ba1	Expected trend		
Combined Solvency Score		baa1		ba1			
Liquidity							
Funding Structure							
Market Funds / Tangible Banking Assets	11.3%	a3	↔	baa1	Deposit quality		
Liquid Resources							
Liquid Banking Assets / Tangible Banking Assets	26.7%	baa2	↔	baa2	Expected trend		
Combined Liquidity Score		baa1		baa1			
Financial Profile							
				baa3			
Qualitative Adjustments				Adjustment			
Business Diversification				0			
Opacity and Complexity				0			
Corporate Behavior				0			
Total Qualitative Adjustments				0			
Sovereign or Affiliate constraint				A2			
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	2	A2	A2	
Counterparty Risk Assessment	1	0	baa1 (cr)	2	A2(cr)		
Deposits	0	0	baa2	2	A3	A3	
Senior unsecured bank debt	0	0	baa2	2		A3	

[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	A2/P-1
Bank Deposits	A3/P-2
Baseline Credit Assessment	baa2
Adjusted Baseline Credit Assessment	baa2
Counterparty Risk Assessment	A2(cr)/P-1(cr)
Senior Unsecured	A3

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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