

ISRAEL DISCOUNT BANK LTD.

Registration no. 520007030

The securities of the corporation are listed for trading on the Tel Aviv Stock Exchange

Abbreviated name: Discount

Address: 23 Yehuda Halevi St., Tel Aviv 6513601, Israel

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Israel Securities Authority
www.isa.gov.il

Tel Aviv Stock Exchange Ltd.
www.tase.co.il

Immediate Report Regarding Rating of Debentures/Rating of Corporation or Withdrawal of Rating

On December 21, 2015, *another*. Moody's, published an *updated* rating report/notice:

1. Rating report or notice

☒ Rating of Corporation: *Another* Moody's.._____ *stable*

Comments/Nature of the Notice: *Rating ratification* _____

Rating history during the three years prior to the rating/notice date:

Date	Subject of Rating	Rating	Comments/Nature of the Notice
30/06/2015	<i>Israel Discount Bank Ltd.</i>	<i>Other</i> <i>Baa1</i> Moody's _____ <i>stable</i>	<i>Outlook/forecast upgrade</i>
18/01/2015	<i>Israel Discount Bank Ltd.</i>	<i>Other</i> <i>Baa1</i> Moody's _____ <i>negative</i>	<i>Rating downgrade</i>
21/10/2014	<i>Israel Discount Bank Ltd.</i>	<i>Other</i> <i>A3</i> Moody's _____ <i>negative</i>	<i>Rating ratification</i>
12/12/2013	<i>Israel Discount Bank Ltd.</i>	<i>Other</i> <i>A3</i> Moody's _____ <i>negative</i>	<i>Rating ratification</i>

☐ Rating of Debentures of the Corporation

Stock

Exchange

Security

Name and Class
of Security

Registration
Number

Rating
Company

Current
Rating

Comments/Nature of the Notice

_____	_____	_____	_____	_____
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Rating history during the three years prior to the rating/notice date:

Name and Class of Security	Stock Exchange Security Registration Number	Date	Class of Security Being Rated	Rating	Comments/Nature of the Notice

Moody's rating report (credit opinion) is presented in the appendix below.

2. On _____, _____ announced that the rating for ..._____ had been withdrawn.

In addition, Moody's has ratified the "Counterparties Risk assessments" rating at a level of A3

This Report has been signed on behalf of the Corporation, in accordance with Regulation 5 of the Securities Regulations (Periodic and Immediate Reports), 5730-1970, by Uri Levin, Senior Executive Vice President and Head of Planning, Strategy and Finance Division and Joseph Beressi, Senior Executive Vice President and Chief Accountant.

Reference numbers of previous documents relating to this topic (their mention does not constitute their inclusion by way of reference):

Prior names of the reporting entity:

Date of updating structure of form: December 15, 2015

Name of person making electronic report: Sokolov-Danoch, Michal; Position: Corporate Secretary
Name of Employing Company:
23 Yehuda Halevi St., Tel Aviv 6513601, Israel, Tel: 972-3-5145582; Fax: 972-3-5171674
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The English translation is prepared for convenience purposes only.
In the case of any discrepancy between the English and Hebrew versions, the Hebrew will prevail.***

APPENDIX

MOODY'S

INVESTORS SERVICE

Credit Opinion: Israel Discount Bank

Global Credit Research - 21 Dec 2015

Tel Aviv, Israel

Ratings

Category	Moody's Rating
Outlook	Stable
Bank Deposits	Baa1/P-2
Baseline Credit Assessment	ba1
Adjusted Baseline Credit Assessment	ba1
Counterparty Risk Assessment	A3(cr)/P-2(cr)

Contacts

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Key Indicators

ISRAEL DISCOUNT BANK (Consolidated Financials)[1]

	[2]9-15	[2]12-14	[3]12-13	[3]12-12	[3]12-11	Avg.
Total Assets (ILS million)	206,914.0	206,946.0	200,507.0	201,012.0	202,472.0	[4]0.5
Total Assets (USD million)	52,718.3	53,179.7	57,766.3	53,874.7	52,951.2	[4]-0.1
Tangible Common Equity (ILS million)	12,953.0	12,684.3	11,506.6	11,038.9	10,154.5	[4]6.3
Tangible Common Equity (USD million)	3,300.2	3,259.5	3,315.1	2,958.6	2,655.6	[4]5.6
Problem Loans / Gross Loans (%)	2.7	2.7	3.7	5.1	5.2	[5]3.9
Tangible Common Equity / Risk Weighted Assets (%)	8.8	8.7	8.4	7.9	7.3	[6]8.7
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	22.9	22.3	32.3	47.2	51.4	[5]35.2
Net Interest Margin (%)	2.2	2.2	2.2	2.3	2.5	[5]2.3
PPI / Average RWA (%)	1.2	0.8	1.3	1.4	1.2	[6]1.0
Net Income / Tangible Assets (%)	0.5	0.3	0.5	0.4	0.5	[5]0.4
Cost / Income Ratio (%)	76.5	83.9	77.4	75.2	77.4	[5]78.1
Market Funds / Tangible Banking Assets (%)	6.2	6.8	6.4	6.9	7.6	[5]6.8
Liquid Banking Assets / Tangible Banking Assets (%)	30.9	31.9	31.6	33.2	34.7	[5]32.5
Gross loans / Due to customers (%)	82.2	80.4	79.9	79.4	77.8	[5]79.9

Source: Moody's

[1] All figures and ratios are adjusted using Moody's standard adjustments [2] Basel III - fully-loaded or transitional phase-in; LOCAL GAAP [3] Basel II; LOCAL GAAP [4] Compound Annual Growth Rate based on LOCAL GAAP reporting periods [5] LOCAL GAAP reporting periods have been used for average calculation [6] Basel III - fully-loaded or transitional phase-in & LOCAL GAAP reporting periods have been used for average calculation

Opinion

SUMMARY RATING RATIONALE

We assign Baa1/Prime-2 deposit ratings to Israel Discount Bank (IDB), Israel's third-largest bank with a 15% market share of total assets. The deposit ratings incorporate a three-notch uplift from the bank's ba1 baseline credit assessment (BCA), based on our assessment of a very high probability of government support in the event of need. We also assign a Counterparty Risk Assessment (CR Assessment) of A3(cr) / Prime-2(cr).

The ratings, and specifically the bank's BCA, are driven by (1) IDB's favourable deposit-based funding structure, with customer deposits accounting for 79% of non-equity funding; (2) its large liquidity buffers with a liquidity coverage ratio of 131.5% as of September 2015; and (3) its moderate capital buffers, on a global basis although higher than most domestic peers, with a Common Equity Tier 1 ratio of 9.5% as of September 2015.

IDB's ba1 BCA also captures its weaker-than-domestic-peers asset quality metrics, with the ratio of non-performing loans (NPLs, defined as impaired loans plus other loans over 90 days overdue) to gross loans of 2.7% as of September 2015, as well as its weak profitability and efficiency metrics with a cost-to-income ratio of 77% for the nine months to September 2015.

Rating Drivers

- Good asset quality on a global basis although weaker than domestic peers
- Moderate, although better than domestic peers, capital buffers
- Weak profitability and efficiency metrics
- Strong retail deposit base and good liquidity
- Israel's Strong Macro Profile
- Very high likelihood of government support, in case of need, underpins the deposit ratings

Rating Outlook

All ratings carry a stable outlook.

What Could Change the Rating - Up

Upward pressure could originate from improvements in the bank's BCA following evidence of materially improved profitability and efficiency metrics, combined with asset quality improvements.

What Could Change the Rating - Down

Negative pressure could be exerted on the ratings if a deterioration in operating conditions leads to a weakening of asset quality, profitability and capital metrics.

DETAILED RATING CONSIDERATIONS

GOOD ASSET QUALITY METRICS ON A GLOBAL BASIS ALTHOUGH WEAKER THAN DOMESTIC PEERS

IDB maintains good asset quality metrics relative to similarly rated banks globally, as it benefits from strong underwriting standards as well as a strict regulatory and legal framework that allows the banks full recourse to the borrowers. Nevertheless with a ratio of NPLs to gross loans of 2.7% as of September 2015 and credit costs standing at 0.27% for Q3 2015, IDB's asset quality metrics are the weakest amongst its rated domestic peers. Further, we expect IDB's credit costs, which were supported in recent quarters at low levels due to cash recoveries, to rise reaching the historical average level of 0.5%-0.6%.

Credit risks remain elevated in IDB's loan book driven by (1) the still high, albeit declining, concentration levels in the bank's loan book, which makes its asset quality vulnerable to a potential deterioration in the financial position of one of its large borrowers; and (2) the increasing credit risk in the mortgage market in Israel, mainly as a result of the sharp property price increases of around 100% in the last 7 years that have outpaced household income growth. These developments render the asset quality of the system's banks vulnerable to interest rate rises or to a potential

weakening in economic activity, which could lead to higher unemployment and a correction in real-estate prices. However, while we have recently revised downwards our forecast for Israel's real GDP growth on account of weaker demand for Israel's exports, we continue to expect meaningful economic expansion of 3.0% for 2016. As of September 2015 mortgages accounted for 17% of IDB's loan book.

MODERATE, ALTHOUGH BETTER THAN DOMESTIC PEERS, CAPITAL BUFFERS

IDB already meets its 9.0% (plus 1% capital add-on against its mortgage portfolio resulting in 9.14% minimum CET 1) regulatory minimum Common Equity Tier 1 (CET 1) capital ratio, which will become effective 1 January 2017: with a CET 1 ratio of 9.5% as of September 2015, the bank's capital buffers are above those of most of its domestic peers. Our scenario analysis shows that the bank can absorb the added credit costs we expect under our central scenario.

However, IDB's capital buffers compare unfavourably with similarly rated banks globally, although we recognise that IDB uses the more conservative "standardised approach" in calculating risk-weighted assets (RWAs). Its RWAs-to-total-assets ratio stands at 71% as of September 2015, higher than the 69% average of similarly rated banks globally and significantly higher than banks and systems using the internal ratings-based (IRB) approach. The average RWAs-to-total-assets ratio for euro-area banks, most of which use the IRB for the RWA calculation, was 41% as of June 2015.

WEAK PROFITABILITY AND EFFICIENCY METRICS

For the nine months to September 2015 IDB reported a 38% year-on-year increase in net income to NIS738 million (USD190 million). The improvement mainly stems from a reduction in expenses, primarily staff costs, reflecting IDB's efforts to control its cost base through the introduction of an early retirement scheme in 2014.

Nevertheless, with an annualised return on RWA of 0.67% and cost to income ratio of 77%, IDB's profitability and efficiency metrics are below its local peers and those of similarly rated banks globally. The pressure on the bank's profitability stems from (1) its high cost base, with operating costs at 2.8% of total assets and its cost-to-income ratio at 77%, which excludes one-off costs; (2) the low interest rate environment, which adversely affects net interest margins; and (3) Israel's high tax rate, with the statutory tax rate at 37.7%.

We acknowledge the management's efforts to address some of these issues via its 2015-19 strategic plan. Specifically, following reductions in the head count and the disposal of non-core assets, management aims to maintain its current cost base and improve the cost-to-income ratio and align IDB's efficiency metrics with its domestic peers as the top line grows.

STRONG RETAIL DEPOSIT BASE AND GOOD LIQUIDITY

The bank maintains a stable deposit-based funding structure. Deposits accounted for 79% of non-equity funding as of September 2015, and primarily comprise of granular retail deposits. We expect the bank to continue to be primarily deposit funded, benefitting from the strong savings culture in Israel. Although the bulk of deposits are of a short-term nature (with this being the main reason for the funding structure adjustments in our scorecard), both domestic and foreign deposits have proven to be stable during past shocks in Israel.

IDB also maintains good liquidity buffers. As of September 2015, cash and interbank balances accounted for 13% of total assets, with securities accounting for an additional 19%. The securities portfolio primarily comprises of A1-rated Israeli government securities (57% of the total), while an additional 21% is invested in mortgage-backed and asset-backed securities of US government agencies. The balance is invested in highly rated fixed-income securities of US and European financial institutions. With the liquidity coverage ratio at 131.5% as of September 2015, IDB already exceeds the 100% minimum requirement effective as of January 2017.

ISRAEL'S STRONG MACRO PROFILE

Discount Bank's Macro Profile is underpinned by the country's competitive and diversified economy, supported by high income levels, gradually improving debt metrics and ample funding. The economy has shown resilience despite extensive geopolitical challenges. The banking sector benefits from the country's strong savings culture, which provides sufficient customer deposits for the banks to avoid reliance on more volatile market funding. Our views of the Israeli operating environment also incorporate our assessment of risks surrounding rising real-estate prices and elevated lending by non-banks such as insurance companies and pension funds, which are weakening banks' credit conditions.

SOURCE OF FACTS AND FIGURES CITED IN THIS REPORT

Unless noted otherwise, data related to system-wide trends is sourced from the central bank. Bank-specific figures originate from the bank's reports and Moody's Banking Financial Metrics. All figures are based on our own chart of account and may be adjusted for analytical purposes. Please refer to the document: "Financial Statement Adjustments in the Analysis of Financial Institutions" https://www.moody's.com/research/Financial-Statement-Adjustments-in-the-Analysis-of-Financial-Institutions--PBC_182293) published on 15 June 2015. The numbers in the key indicators table at the top of the page do not reflect restatements carried out by the bank to prior years financials.

Notching Considerations

GOVERNMENT SUPPORT

We assume a very high likelihood of government support for Discount Bank's rated deposits. This assumption reflects the Israeli government's longstanding practice of injecting capital into systemically important banks in case of need, rather than using resolution tools or allowing the institution to enter bankruptcy. This assumption is particularly applicable to Discount Bank given its 15% share of the domestic market, and hence the material systemic consequences of an unsupported failure. We therefore incorporate three notches of government support into the bank's deposit ratings (Baa1).

CR ASSESSMENT

The CR Assessment is positioned at A3(cr)/Prime-2(cr). The CR Assessment, prior to government support, is positioned one notch above the Adjusted BCA of ba1, reflecting our view that its probability of default is lower than that of deposits. We believe senior obligations represented by the CR Assessment will be more likely preserved in order to limit contagion, minimise losses and avoid disruption of critical functions.

The CR Assessment also benefits from three notch of systemic support, in line with our support assumptions on deposits. This reflects our view that any support provided by governmental authorities to a bank which benefits deposits is very likely to benefit operating activities and obligations reflected by the CR Assessment as well, consistent with our belief that governments are likely to maintain such operations as a going-concern in order to reduce contagion and preserve a bank's critical functions.

About Moody's Bank Scorecard

Our 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 Factors

Israel Discount Bank

Macro Factors	
Weighted Macro Profile	Strong

Financial Profile						
Factor	Historic Ratio	Macro Adjusted Score	Credit Trend	Assigned Score	Key driver#1	Key driver#12
Solvency						
Asset Risk						
Problem Loans / Gross Loans	3.5%	baa1	← →	baa3	Sector concentration	Single name concentration
Capital						
TCE / RWA	8.8%	ba3	← →	ba3	Risk-weighted capitalisation	Stress capital resilience

Profitability Net Income / Tangible Assets	0.4%	ba1	← →	ba2	Earnings quality	
Combined Solvency Score		ba1		ba2		
Liquidity Funding Structure Market Funds / Tangible Banking Assets	6.8%	a1	← →	baa1	Deposit quality	
Liquid Resources Liquid Banking Assets / Tangible Banking Assets	31.3%	a3	← →	a3	Stock of liquid assets	
Combined Liquidity Score		a2		baa1		

Financial Profile	ba1
Qualitative Adjustments	Adjustment
Business Diversification	0
Opacity and Complexity	0
Corporate Behavior	0
Top Qualitative Adjustments	0
Sovereign or Affiliate constraint	A1
Scorecard Calculated BCA range	baa3 - ba2
Assigned BCA	ba1
Affiliate support notching	0
Adjusted BCA	ba1

Instrument Class	Loss Given Failure notching	Additional notching	Preliminary Rating Assessment	Government Support notching	Local Currency rating	Foreign Currency rating
Deposits	0	0	ba1	3	Baa1	Baa1

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