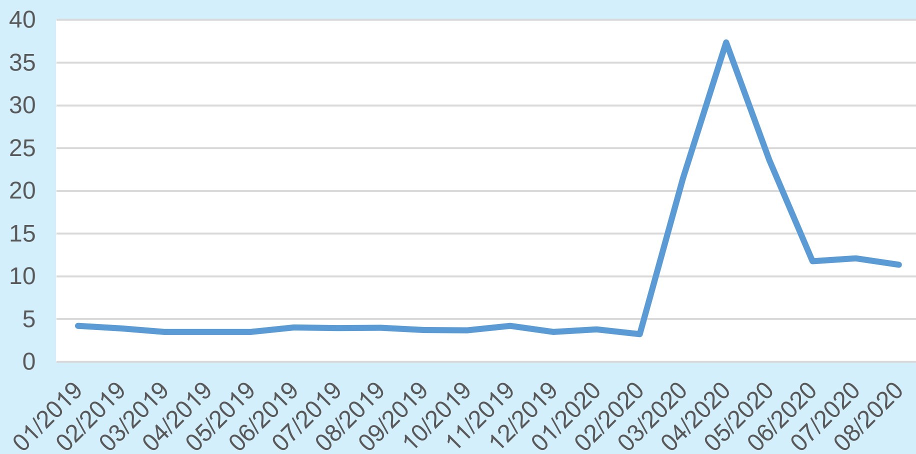
BANK OF ISRAEL
Banking Supervision Department

Survey of the Banking System – First Half of 2020

Introduction

During recent months, Israel and the rest of the world have been in upheaval as a result of the COVID-19 pandemic. The onset of the pandemic led, among other things, to a significant decline in economic activity within a relatively short period. Within a few weeks, the unemployment rate had risen to unprecedented levels and the GDP in Israel and worldwide experienced a major contraction.

Figure 1
The Broad Unemployment Rate*, Ages 15+, 2019–August 2020 (percent)



* Includes the unemployed, the employed who are temporarily absent due to causes associated with the pandemic (including unpaid leave), and nonparticipants who stopped working due to dismissal or closure of their workplace during the pandemic.

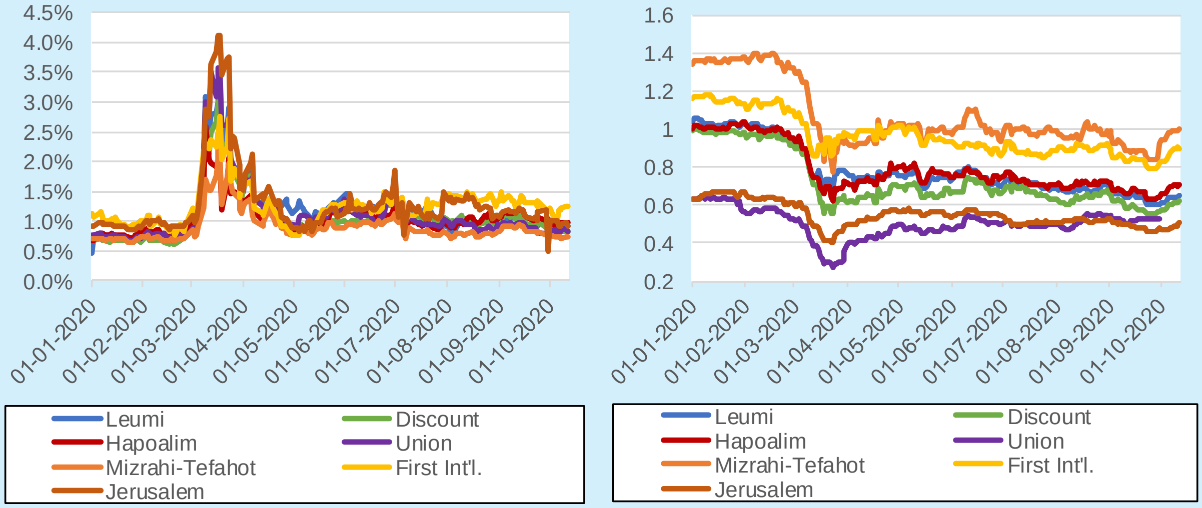
SOURCE: Central Bureau of Statistics Labor Force Survey.

The Bank of Israel and the Banking Supervision Department have taken a number of important steps in order to minimize the crisis's effect on the public, and have assisted Israeli banks by means of various regulatory tools in order to support economic growth and minimize the harm to the banks' customers as much as possible. (For further details on the measures taken during the first months of the crisis, see Box 3.1 of the *Survey of Israel's Banking System* for 2019. For further details on the steps taken later on, see Box 1 of this survey.)

Figure 2

Bond Spreads in the Banking System, January–October, 2020

Market Value over Book Value (MV/BV), the Banking System, January–October, 2020



This survey presents the Israeli banking system's results for the first two quarters of 2020. At this stage, the macroeconomic situation's effect on the banks' balance sheets and financial statements is manifested in a number of ways. First, the volatility in the markets has affected the banks' performance and balance sheets. In addition, the banks have significantly increased their credit loss provisions (primarily group losses), which reflects an expectation of future credit losses. Finally, the program to defer loan repayments is having an effect on the structure of their revenues and cash flows.

From a forward-looking perspective, there is still a high level of uncertainty regarding the pandemic's effect on the economy, which is dependent on the response to the virus. In this context, there are many scenarios of differing intensity and duration of the effect of mitigation policy on the economy. During these months, the Banking Supervision Department has carried out an evaluation using macroeconomic stress tests for the banking system, based on a uniform scenario that includes a deterioration in morbidity in Israel and a return to the restrictions placed on economic activity. The results of the test indicate that the banking system is expected to experience significant losses if the crisis worsens, originating primarily in the portfolio of consumer and business credit. However, these losses will not affect the banking system's ability to continue supporting economic activity during the crisis and thereafter. These results illustrate the strength and stability of the Israeli banking system in general, and of each of the banks in the system. (For further details on the test and its results, see Box 2 in this survey.)

Business results and efficiency

Business results

The net profit of the five largest banks fell significantly during the first half of 2020 relative to the same period in the previous year (by 62 percent)[1] as a result of the effects of the COVID-19 crisis, and stood at about NIS 2,296 million (Table 2). The return on equity stood at about 4.3 percent, which is its lowest level since 2008, as compared to about 10.7 percent during the same period in 2019 and about 8.3 percent in 2019 as a whole (Figure 2). Net profit during the reviewed period was adversely affected by the significant rise in loan loss provisions (about 375 percent)[2] and the declines in net interest income (about 5.3 percent) and noninterest financing income (about 26 percent). The drop in net profit was somewhat offset by the increase in income from fees (about 2 percent) and a slight drop in operating expenses (about 5 percent), which was the result of a decline in salaries and salary-related expenditure (about 9 percent), due partly to the decrease in provisions for grants against the background of the decline in the system's financial results.

The increase in loan loss provisions encompassed all of the banks and was reflected in an increase in group and individual provisions as part of the COVID-19 crisis's effect on the macroeconomic environment and the repayment ability of borrowers in the various segments. (For further discussion, see the section on the credit portfolio.)

Noninterest income declined by about 4.5 percent during the first half of the year relative to the first half of 2019. The decline was a result of the sharp drop of about 26 percent in noninterest financing income relative to the same period in 2019, which was led by the decline in income from shares and exchange rate differentials (Table 2). The decline was partly the result of a fall in the market value of shares in the capital market, particularly at the end of the first quarter of the year. Share values began to partially recover during the second quarter. On the other hand, the decline was offset by a significant increase in financing income from bonds, which was partly the result of the increase in profits from the sale of bonds, and activity in derivatives used to hedge the banks' total exposure, particularly to exchange rate differentials. Another factor that offset the drop in noninterest income was the increase in income from fees, which rose by about 2 percent relative to the same period in 2019. The growth in fees during the first half of the year relative to last year was due to the increase in activity in securities and to exchange rate differentials, primarily during the first quarter of the year, with the onset of the pandemic in Israel. The growth in the level of activity and in fees income encompassed all of the banks except for Discount Bank.

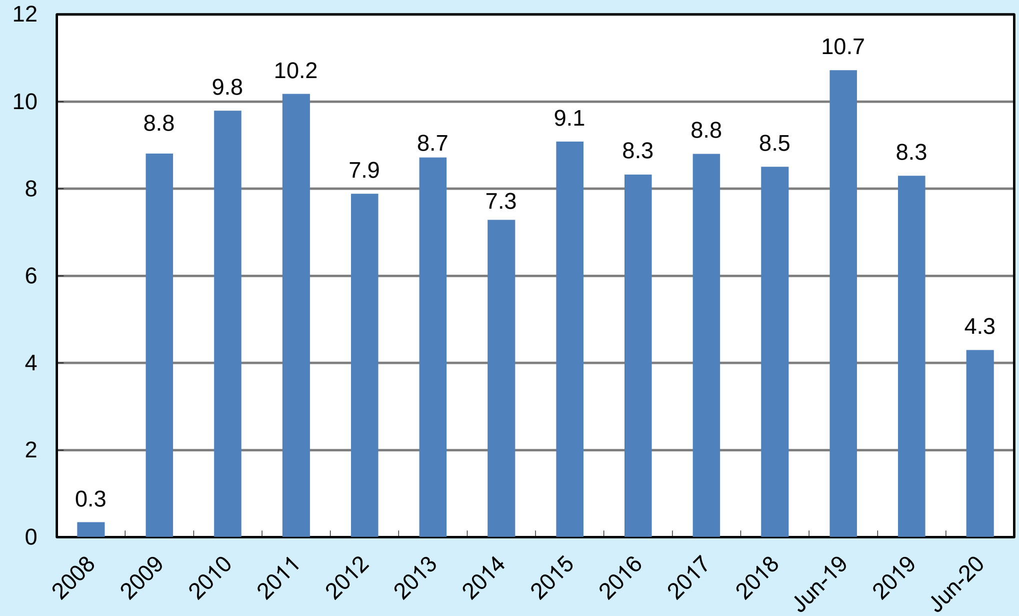
The contraction in net interest income during the reviewed period occurred despite the significant increase in the quantity of interest-bearing assets (about 16 percent). The price effect was negative and constituted the main component behind the drop in income (Table 3), and was the result of several factors: more rapid growth in credit to segments producing a relatively low yield, including

[1] In this survey, rates of change are calculated in annual terms unless specificized otherwise. In general, the rate of change is calculated relative to the parallel period during the previous year or relative to the end of the previous year, as mentioned in the text, and is converted into annual rates, as stated for each calculation.

[2] Calculated as the rate of change in total loan loss provision during the reviewed period relative to the same period in 2019.

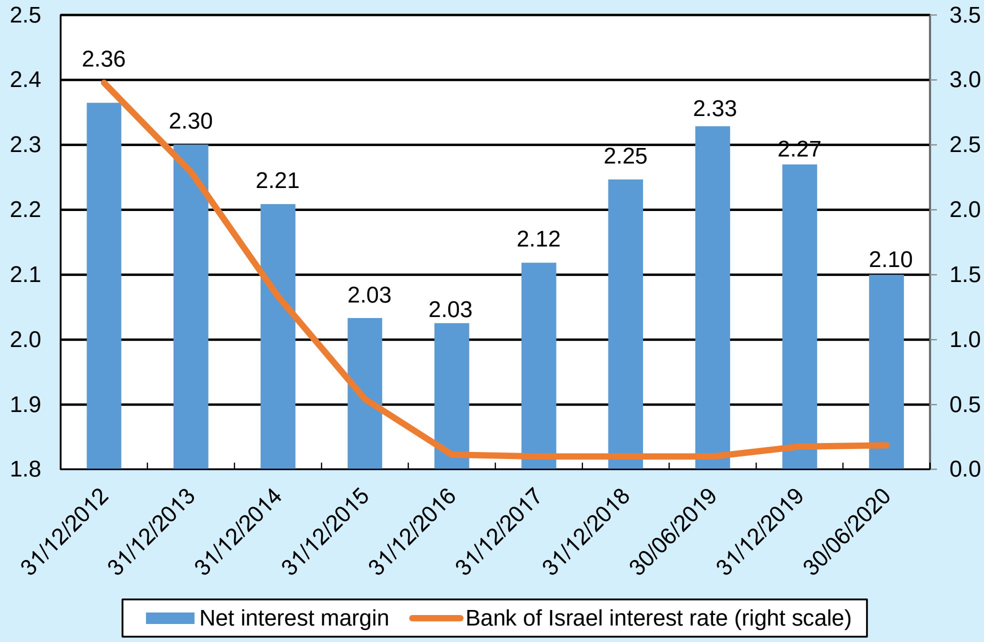
housing credit and small business credit by way of the State Guarantee Fund, which has a low rate of interest relative to small business credit not by way of the fund (for further details, see the section on credit); a large shift of income-producing assets to more liquid investment channels (at central banks) that have a lower yield (for further details, see the section on balance-sheet activity); and a 0.15 percentage point reduction in the Bank of Israel interest rate at the beginning of the second quarter, which also affected interest income in the various segments. The negative price effect on net interest income was offset by the positive quantity effect, which was primarily due to the growth in credit to the public, in addition to the drop in financing expenses on the banks' liabilities. As a result, there was a narrowing of the interest rate gap relative to the same period in 2019 (Figure 5) and in the financial spread, which reflects the ability of the bank to produce a return from interest-bearing activity (Figure 4).

Figure 3
Return on Equity (ROE) After Tax, the Five Banking Groups, 2008–June 2020
(percent)



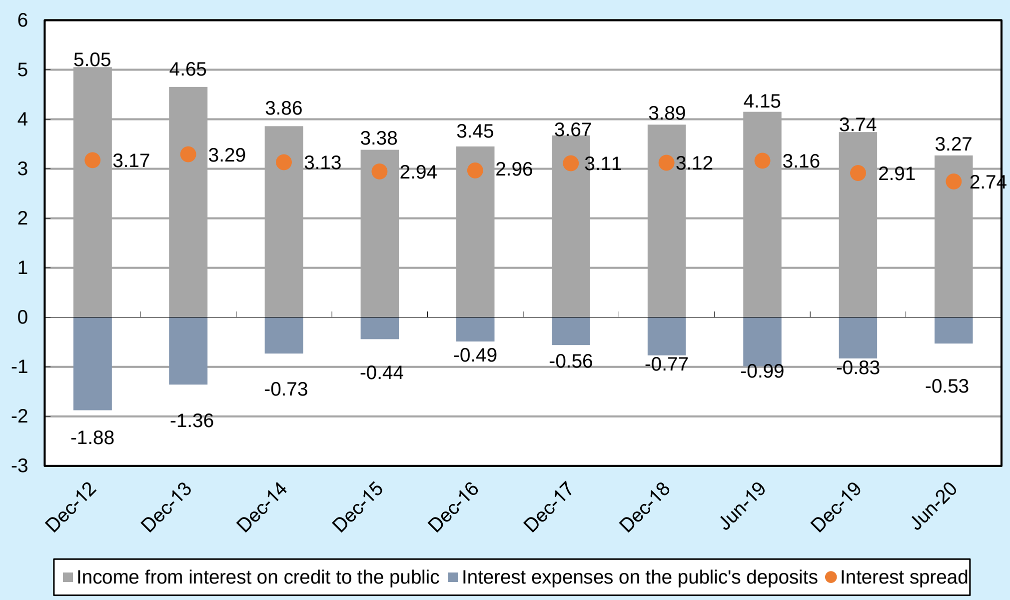
SOURCE: Based on published financial statements.

Figure 4
Net Interest Margin[a] and the Bank of Israel Interest Rate[b], the Five Banking Groups, 2008–June 2020 (percent)



[a] The ratio between net interest income and total monetary assets that generate financing income.
[b] Yearly average. The data for March are calculated as a 3-month average.
SOURCE: Based on published financial statements.

Figure 5
Income from Interest on Credit to the Public, Interest Expenses on the Public's Deposits, and the Interest Rate Spread, the Five Banking Groups, 2012–June 2020 (percent)



SOURCE: Based on published financial statements.

Operational efficiency

Efficiency: The operational efficiency ratio[3] rose slightly during the first half of the year (to 58 percent; Figure 6) relative to the same period in 2019 (57.8 percent), while the output unit cost[4] declined (to 1.62 percent; Figure 7) relative to the first half of 2019 (1.8 percent; Table 4). The partial improvement in the efficiency ratios was achieved as a result of the drop in operational expenses, which was partly due to the decline in salary expenses, primarily in the payment of grants due to a decline in the banks' results in the previous quarter. Bank Leumi, which presented an unusually poor efficiency ratio of 74.7 percent in the first quarter (due to losses it incurred in noninterest financing income), improved its ratio during the first half of 2020 to 57.7 percent. (Although it showed an increase relative to last year, the efficiency ratio in 2019 was positively affected by one-off revenues due partly to the sale of Leumi Card; Figure 6.) This was partly due to a large profit (about NIS 690 million) from noninterest financing income that offset all of the losses in this category for the first quarter of the year. In all the rest of the banking group, there was a moderate improvement in the efficiency ratio relative to the same period in 2019. The sharp improvement in the efficiency ratio at Bank Hapoalim (relative to the end of 2019) is due to the bank's one-off expenses during the second half of 2019, as a result of the settlement reached with the American authorities (Figure 6).

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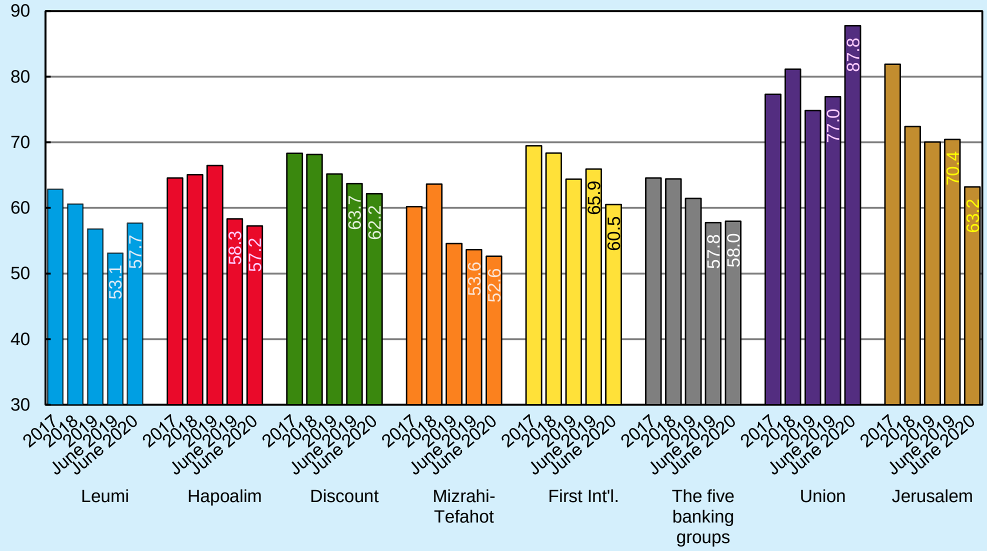
[3] The ratio of total operating and other expenses to total net interest and noninterest income (cost-to-income ratio).

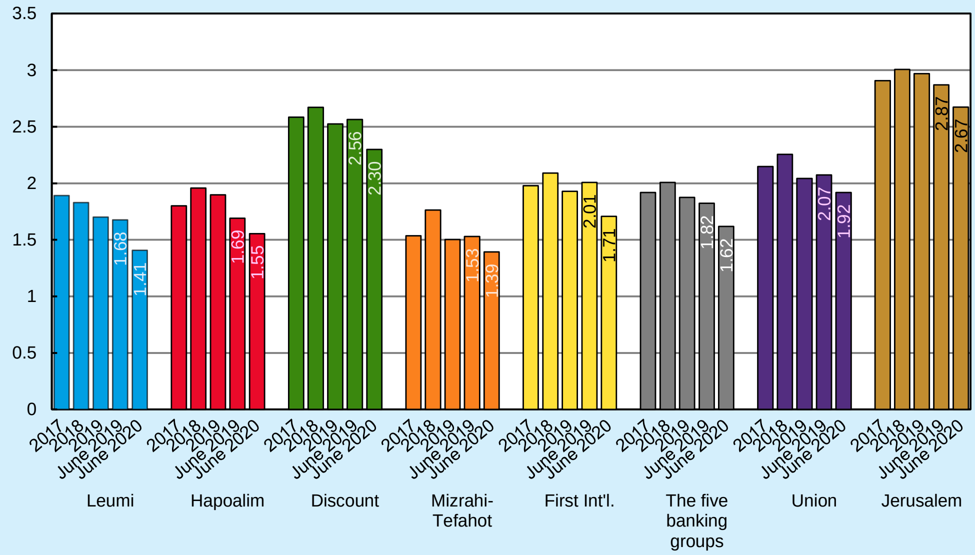
[4] The ratio of total operational and other expenses to average total assets (average cost ratio).

Figure 6
Efficiency Ratio[a] in the Banking System, 2017–June 2020 (percent)



[a] The ratio between total operating and other expenses and total net interest and noninterest income (cost to income).
SOURCE: Based on published financial statements and reports to the Banking Supervision Department.

Figure 7
Output Unit Cost[a] in the Banking System, 2017–June 2020 (percent)



[a] The ratio between total operating and other expenses and average balance of assets (average cost).
SOURCE: Based on published financial statements and reports to the Banking Supervision Department.

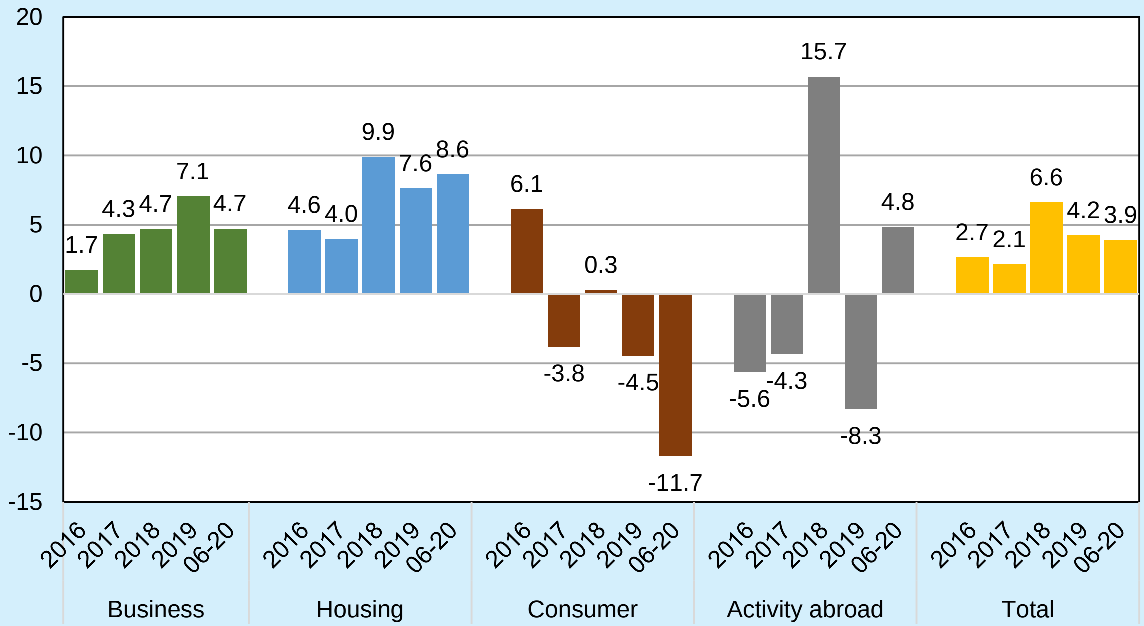
Risks to the banking system

The credit portfolio and credit risk

The credit portfolio

During the first half of 2020, the outstanding credit of the five banks grew by 3.9 percent (in annual terms; Figure 8). Commercial credit (4.7 percent) and housing credit (8.6 percent) continue to be the main sources of growth in the credit portfolio, in view of the acceleration of the downward trend in consumer credit (-11.7 percent). It is worth mentioning that this growth occurred despite the contraction in credit to the public of about NIS 10.2 billion (about 1 percent) in the second quarter relative to the first quarter, 80 percent of which was due to the drop in commercial credit following a sharp jump during the first quarter. The deterioration in the macroeconomic situation had an impact on the ability of households and businesses to meet their commitments to the banking system, which led to lower quality indices of the credit portfolio.

Figure 8
Rate of Change in Outstanding Balance-Sheet Credit to Principal Segments, the Five Banking Groups, December 2015–June 2020 (percent)



[a] The declines in consumer credit at the end of 2018 and in June 2019 are due to retroactive corrections of the sale of the "Max" credit card company from Leumi Group.

SOURCE: Based on published financial statements and reports to the Banking Supervision Department.

Consumer credit

The slowdown in economic activity and the imposition of the COVID-19 restrictions led to a contraction of the banking system's consumer credit portfolio by about 11.7 percent. A large part of the drop—about 40 percent (NIS 3 billion)—came from deferred credit between the date of a purchase and the date of the credit card debit, in view of the decline in credit card purchases. The contraction in the portfolio occurred against the background of about NIS 1.9 billion in loan repayment deferrals, which constituted an alternative source of credit for households that had experienced a drop in their income as a result of the COVID-19 crisis. The decline in consumer credit was apparently the result of both the drop in the public's economic activity and in demand for consumer credit as a result of the crisis and the lower exposure of the banking system to this type of credit during the two years previous to the crisis, as part of the change in the credit portfolio mix (Figure 8). As in the case of the banking system, negative growth was also observed during the first half of 2020 among nonbank entities. Thus, the credit card companies' portfolio of credit to individuals shrank during the reviewed period by about 1.3 percent, compared to growth of 8.1 percent during the same period in 2019 and 14.3 percent during 2019 as a whole.

Loan loss provisions stood at 1.64 percent, and impaired credit and credit in arrears of more than 90 days as a share of total credit to individuals stood at 1.36 percent (compared to 0.57 percent and 1.24 percent, respectively, at the end of 2019; Table 7).

Housing credit

During the first nine months of 2020, there was a large volume of loans provided relative to the same period last year (NIS 56.6 billion as compared to NIS 50.5 billion in 2019), which was a record year for the provision of mortgages (Figure 9). The volume of loans provided in March was about NIS 8.7 billion, which is about 21 percent higher than the previous record level in December 2019.

In this context, the average size of a new loan since the beginning of the year stood at about NIS 760 thousand, an increase of about 8 percent relative to the average for 2019. Loans to first-time home buyers as a share of total housing loans remained stable (at about 50 percent), partly in view of an increase in the proportion of loans provided within the framework of the “Buyer’s Price” program, both as a share of total loans provided (an average of 15 percent during 2020 as compared to 12 percent in 2019[5]) and as a share of total housing loans provided (an average of about 20 percent in 2020 as opposed to about 15 percent in 2019), as a result of the maturing of rights won in Buyer’s Price lotteries to the stage of actually taking out a loan.

During the crisis, the Banking Supervision Department allowed the banks to provide all-purpose loans using a home as collateral at an LTV rate rate of up to 70 percent (as opposed to 50 percent normally). In view of this change, in recent months (May to September) there was a slight increase in the proportion of all-purpose loans as a share of total loans provided with a home as collateral, both in total credit (7.4 percent as opposed to an average of about 6 percent in recent years; Figure 11) and in the number of transactions (18.6 percent as opposed to an average of about 17 percent in recent years).

The interest rate on mortgages returned to almost its pre-crisis level (Figure 12). Thus, in September 2020, the average weighted interest rate on mortgages stood at 2.54 percent as compared to 2.51 percent in February 2020. This followed a sharp increase in April (when it reached 2.79 percent). The drop in the interest rate was made possible by, among other things, the lower volatility in the capital market and the steps taken by the Bank of Israel,[6] which led to a decrease in the banks’ cost of raising capital (Figure 13).

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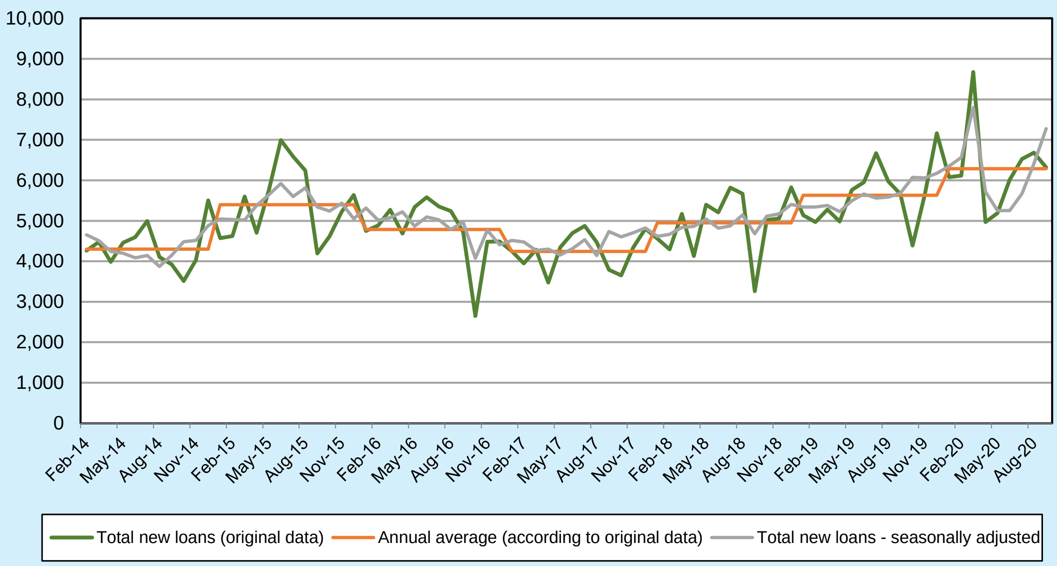
[5] Data on loans provided as part of the Buyer’s Price program are available from March 2019 onward.

[6] “The Bank of Israel puts additional monetary instruments into operation: A plan to increase the supply of credit to small businesses, and repo transactions with corporate bonds as security”
https://www.boi.org.il/en/NewsAndPublications/PressReleases/Pages/6-4-2020.aspx
“The Bank of Israel announces an additional set of steps to expand the monetary response to the coronavirus crisis”

These developments are also reflected in the quality of the housing credit portfolio. The COVID-19 crisis led to an increase in the risk of the portfolio. Although the deferral of mortgage payments is helping many distressed households to weather the crisis, it is creating uncertainty for the banking system with respect to the ability of borrowers to meet their commitments after the deferral period (the total amount of credit for which payments were deferred stood at about 25 percent of the total portfolio in May). In recent months, many borrowers have resumed making the monthly payments on their mortgage, a trend that is reflected in the declining level of credit in grace. Thus, as of July 2020, the quantity of credit in grace was 12 percent as opposed to 25 percent at its peak, which occurred in May, although this level is still high relative to the average of about 3 percent during the last two years (Figure 14) and higher than the pre-crisis level. In parallel, the upward trend in the LTV ratio continued this year, from 52 percent on average in 2019 to 53.7 percent in 2020. This can be explained by the increased proportion of Buyer's Price borrowers, whose LTV rates are generally higher than those of the rest of the population. The payment-to-income (PTI) ratio remained steady (26.4 percent on average since the beginning of the year, as compared to an average of 26.1 percent in 2019), and there was a slight increase in the average term to maturity, which stood at 22.4 years compared to 22 years in 2019. The deferral of payments on housing credit is reflected in the increase in risk originating from these loans, and the increase in the portfolio's risk indices led to an increase in loan loss provisions from 0.03 percent at the end of 2019 to 0.33 percent in the second quarter of 2020 (Figure 16).

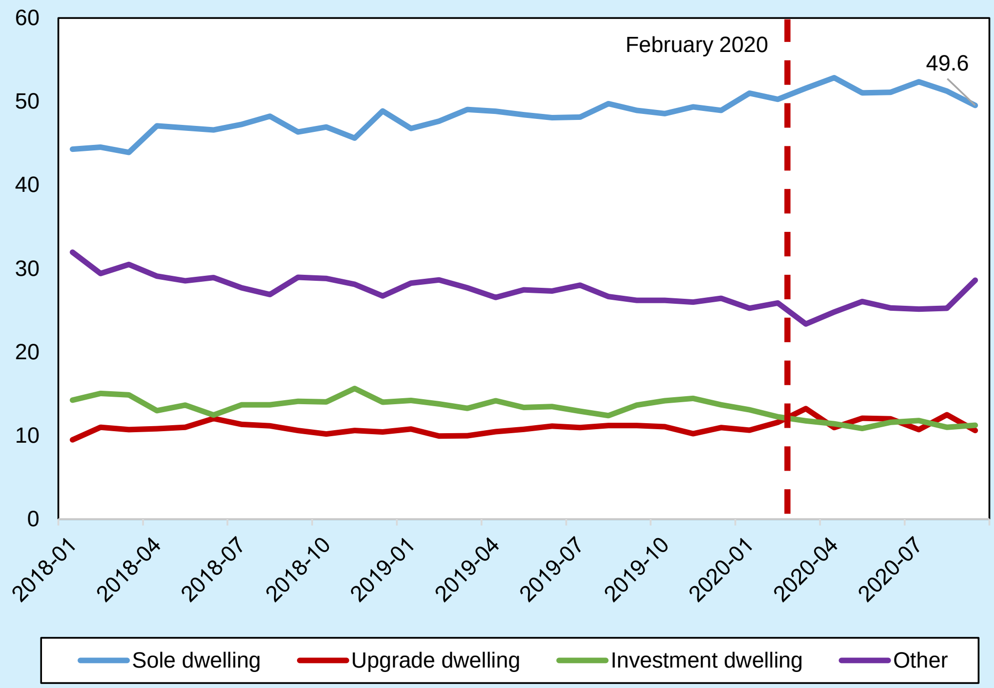
Figure 9
Monthly New Residential Loans and Yearly Average, the Total Banking System, February 2014–September 2020 (NIS million)



SOURCE: Based on reports to the Banking Supervision Department.

https://www.boi.org.il/en/NewsAndPublications/PressReleases/Pages/6-7-2020.aspx

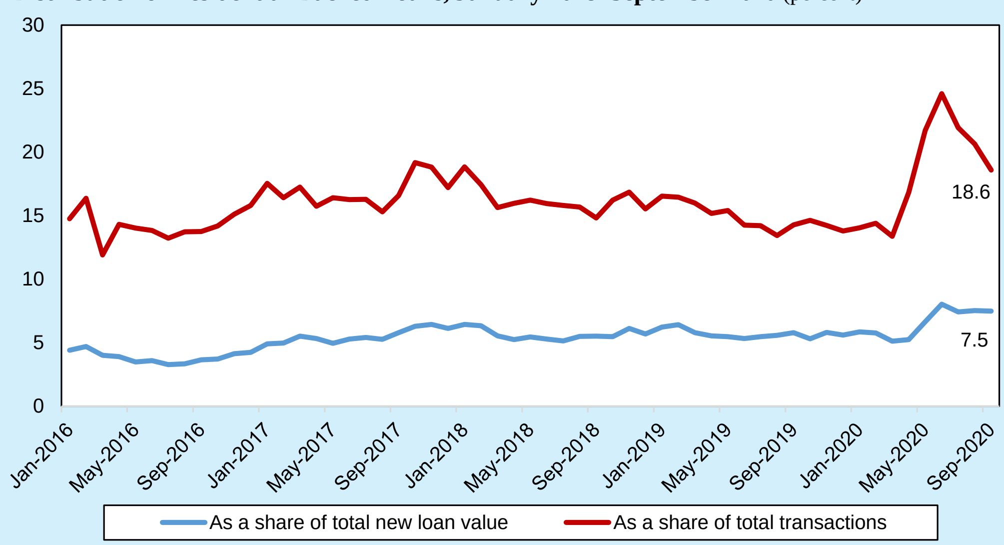
Figure 10
Distribution of the Housing Credit by Purpose, 2018–September 2020 (percent)



[a] Other residential loans for which the bank does not require a declaration from the borrower (loans issued at LTV rates of less than 50 percent).

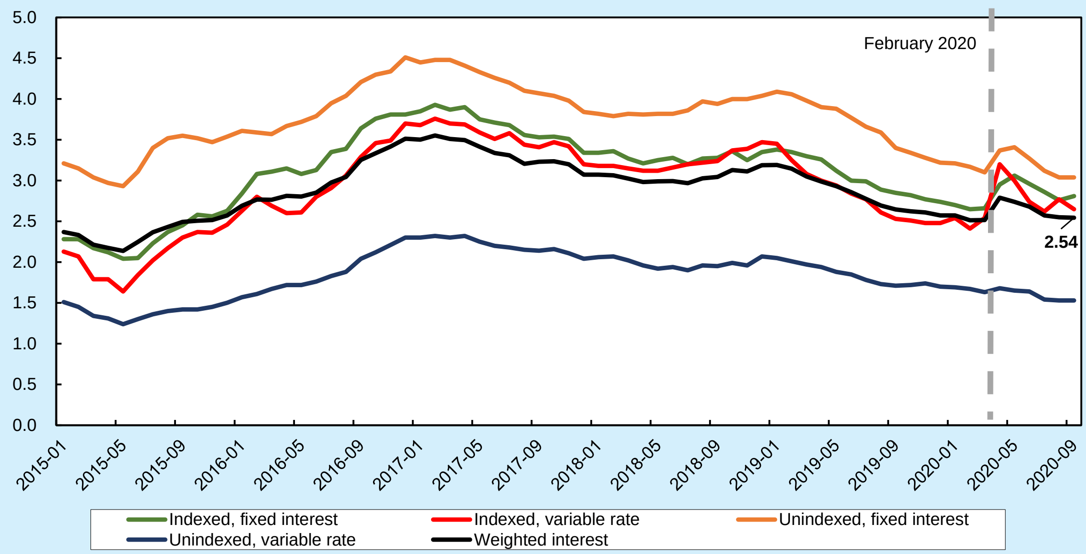
SOURCE: Based on reports to the Banking Supervision Department.

Figure 11
Distribution of Residential-Backed Loans, January 2018–September 2020 (percent)



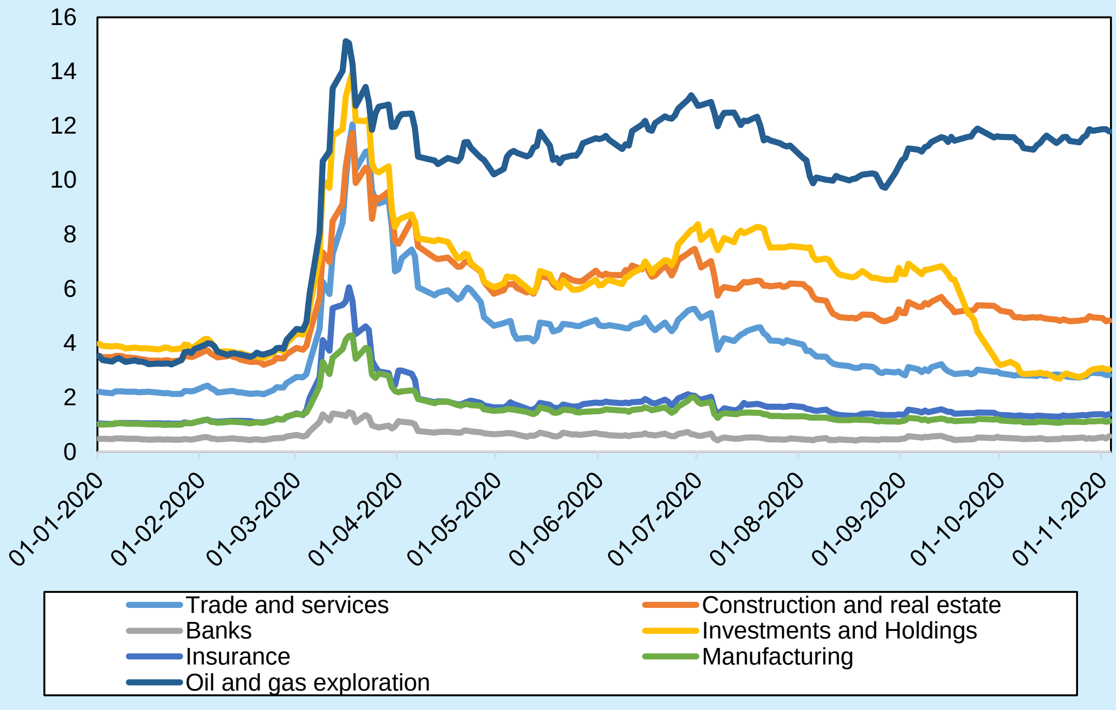
SOURCE: Based on reports to the Banking Supervision Department.

Figure 12
Interest on Residential Loans by Interest and Indexation Track, Total Banking System January 2015–September 2020
(percent)



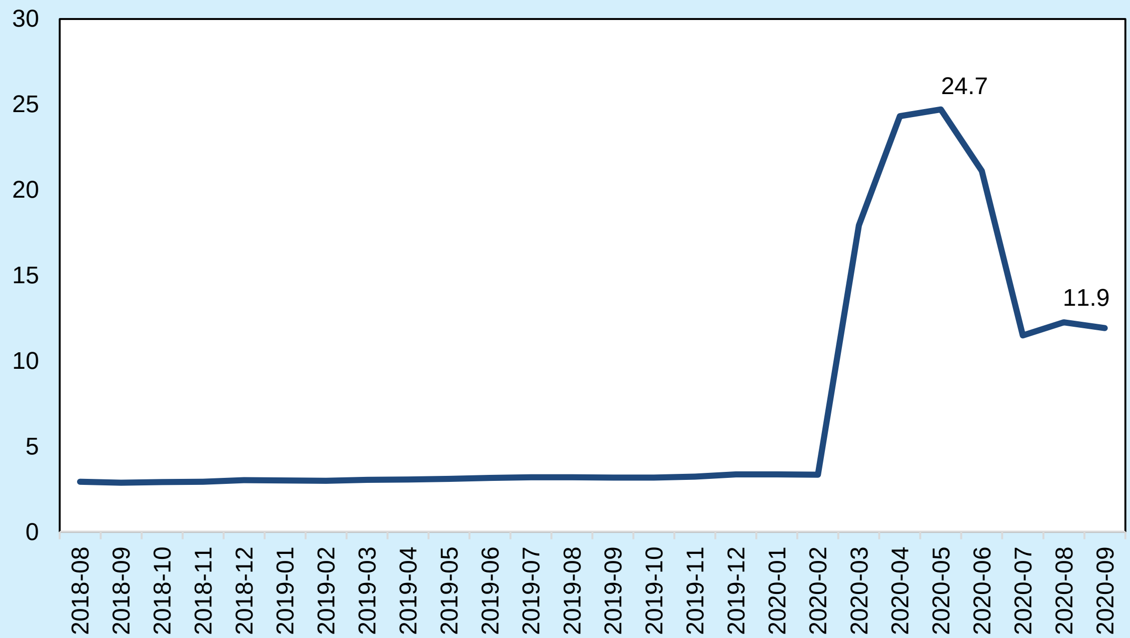
SOURCE: Based on reports to the Banking Supervision Department.

Figure 13
Spreads on Unindexed Bonds from the Zero Curve, January–November 2020 (percent)



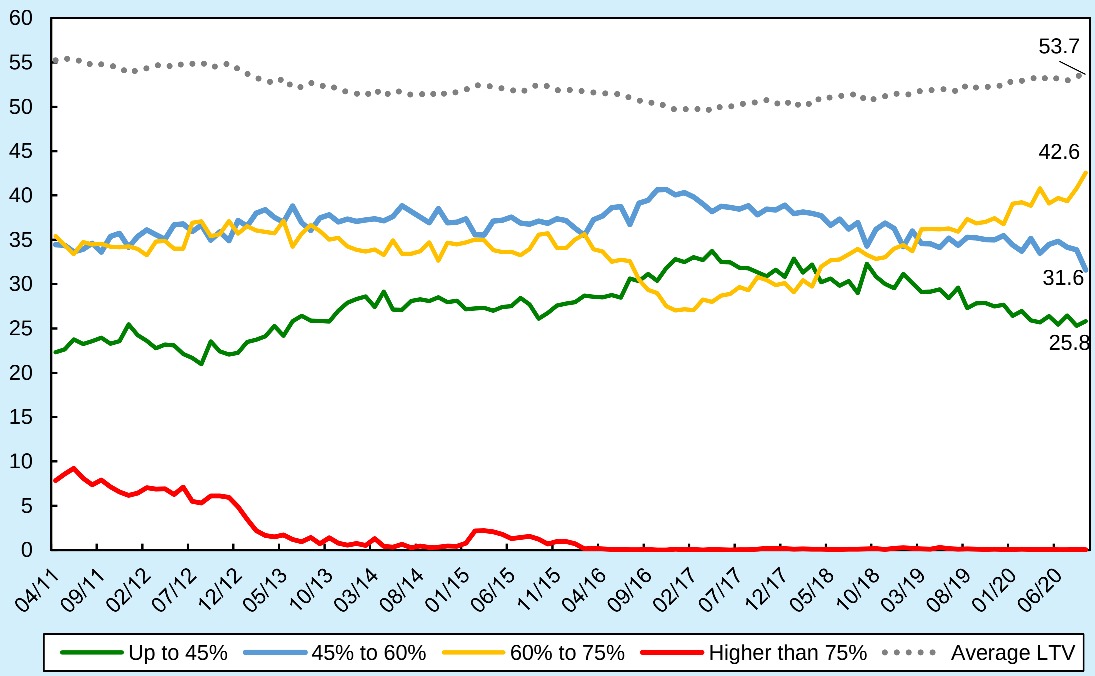
SOURCE: Bank of Israel.

Figure 14
Loan Repayment Deferral Rate, August 2018–September 2020



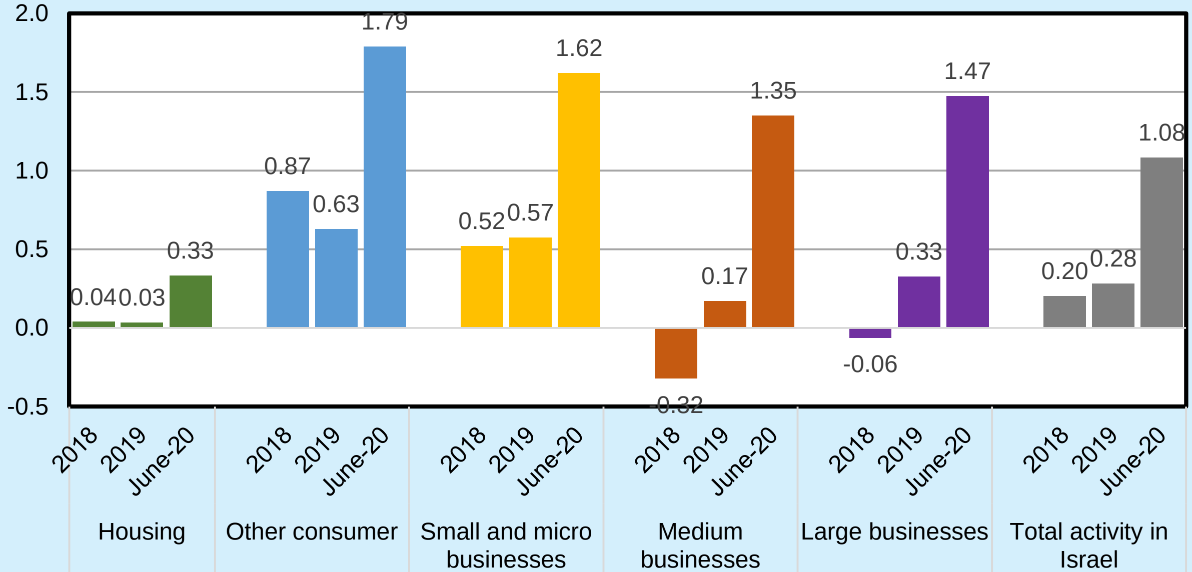
SOURCE: Based on reports to the Banking Supervision Department.

Figure 15
Distribution of New Mortgages by LTV Rate, Total Banking System, April 2011–September 2020
(percent)



SOURCE: Reports to the Banking Supervision Department.

Figure 16
Loan Loss Provisions on Credit in the Various Activity Segments, the Five Banking Groups, December 2018–June 2020 (end-of-period balance, percent)



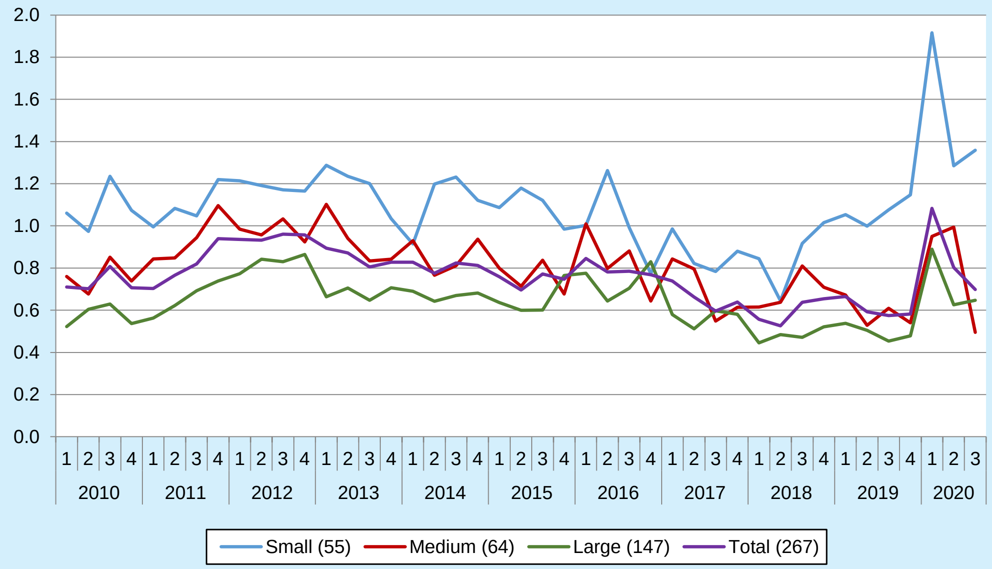
SOURCE: Based on published financial statements and reports to the Banking Supervision Department..

Commercial credit

The growth in commercial credit[7] stood at 4.7 percent since the beginning of the year (Table 5), about 75 percent of which was due to the construction and real estate industry. The credit to the financial services industry declined by about NIS 4.5 billion (15.7 percent), about 80 percent of which was due to the reduction in credit to the industry provided by Bank Leumi of about NIS 2.6 billion (which mainly occurred in the second quarter of 2020). Business credit[8] grew during the first half of 2020 by about 6.6 percent (Table 10), despite a drop of 1.4 percent during the second quarter. The contraction in business credit was due the high level of repayments by businesses that took out credit at the beginning of the crisis. This was in parallel to the reduced difficulty in obtaining financing in the business sector, as reflected in the Companies Survey (Figure 17). The reduced difficulty in obtaining financing is reflected in, among other things, the rates of interest in the banking system, which are low relative to their pre-crisis level (Figure 18).

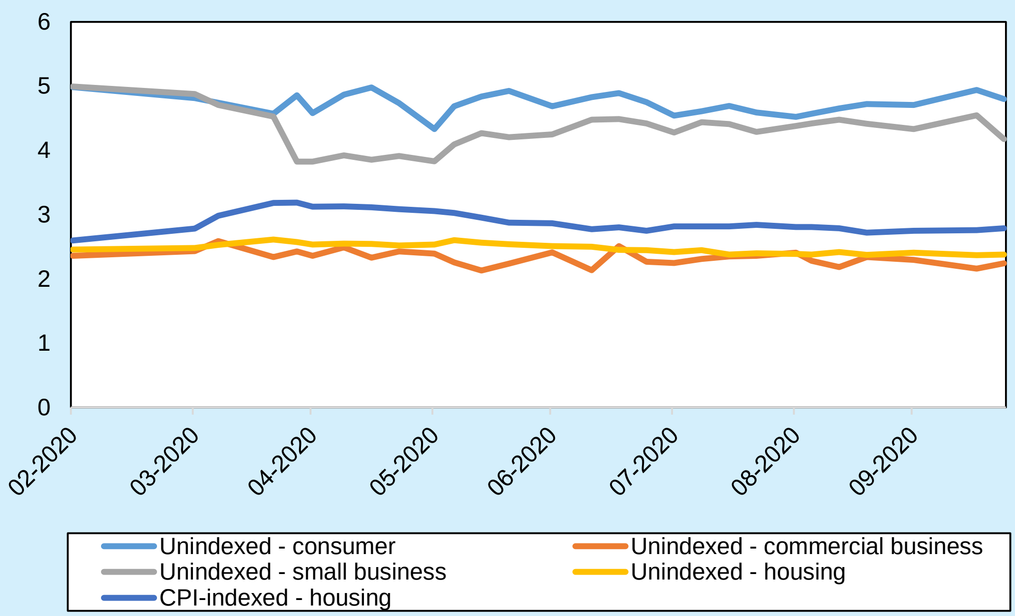
[7] In a breakdown according to industry, commercial credit is defined as the total amount of credit to borrowers that are not categorized as private individuals. When examining credit risk according to activity segment, business credit is defined as total credit that is not categorized as credit to households or private banking.
[8] According to the Banking Supervision Department's classification of activity segments.

Figure 17
Companies Survey[a]: Financing Constraint by Company Size - Business Sector, 2010–September 2020
(weighted by the industry's weight in business sector output, index)



[a] The index reflects the severity of constraints as reported by the companies on a scale ranging from 0 (no constraint) to 4 (severe constraint).
SOURCE: Bank of Israel.

Figure 18
Weighted Interest on New Loans, Shekel Segment[a], February–October 2020
(percent)

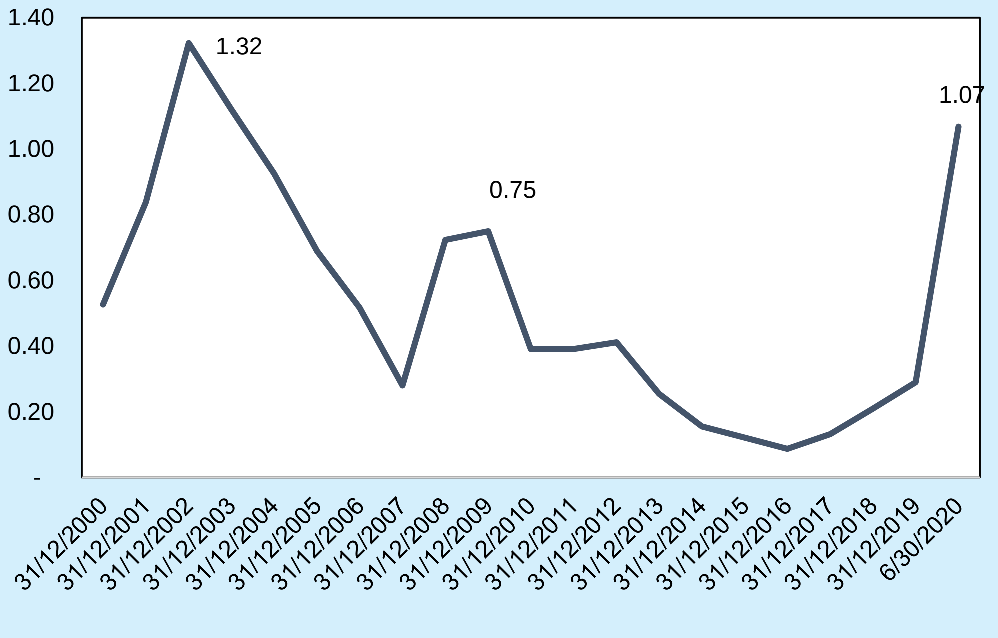


[a] Divided into segments according to the management's approach.
SOURCE: Based on published financial statements and reports to the Banking Supervision Department.

Quality of the credit portfolio

The deterioration in the macroeconomic situation and the state of households and businesses led to a steep rise in loan loss provisions during the year (Figure 19). Thus, during the second quarter of 2020 loan loss provisions amounted to about 1.07 percent of total credit (as opposed to 0.25 percent on average during the two years prior to the crisis). An examination of the composition of the loan loss provision shows that, as in the first quarter, the main source of the provision is the group provision, which was about NIS 3 billion in the second quarter and which constitutes about 83 percent of the total provision. The deterioration in the quality of the credit portfolio can also be seen in the write-off ratio of 0.24 percent and the weight of problematic credit, which stood at 2.45 percent (as compared to 0.16 percent and 2.33 percent, respectively, in 2019; Table 7).

Figure 19
Loan Loss Provisions as a Share of Total Balance-Sheet Credit to Principal Segments, the Five Banking Groups, December 2000–June 2020 (percent)



SOURCE: Based on published financial statements and reports to the Banking Supervision Department.

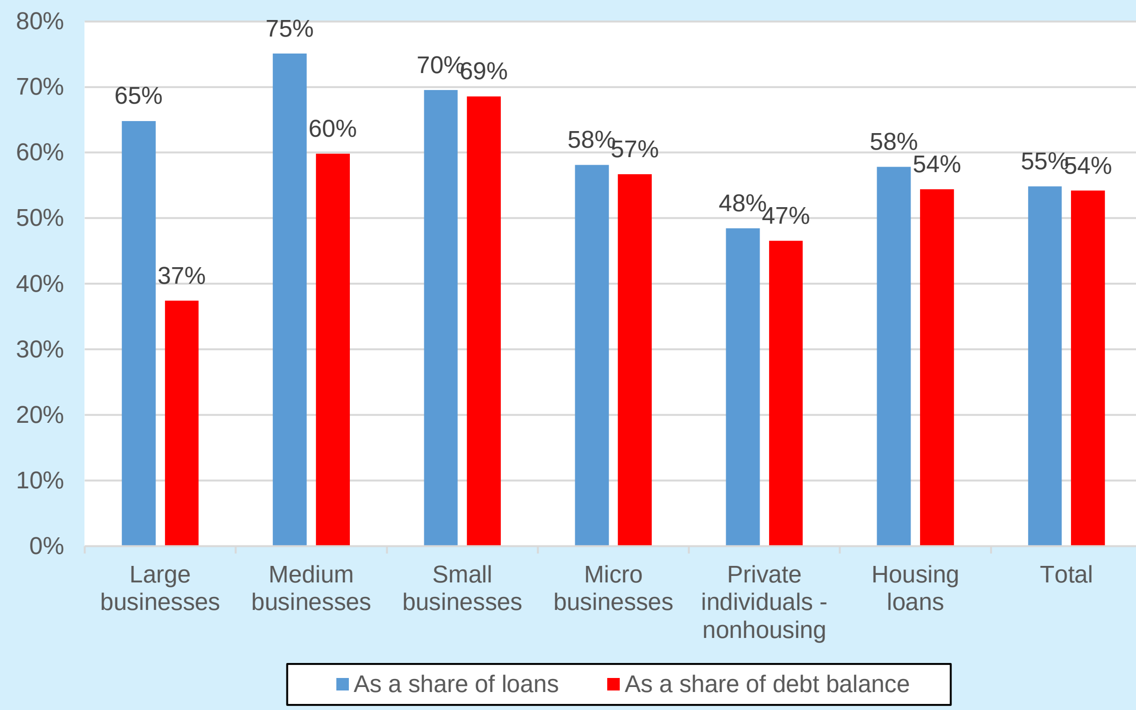
Deferral of payments

In May, the banking system adopted a comprehensive plan for the deferral of loan repayments in order to assist the banks' customers in coping with the impact of the COVID-19 crisis.[9] The data

[9] "The Banking Supervision Department announces a comprehensive framework that has been adopted by the banking system for deferring loan payments as assistance to bank customers in dealing with the ramifications of the coronavirus crisis"
https://www.boi.org.il/en/NewsAndPublications/PressReleases/Pages/7-5-2020b.aspx;
"The Banking Supervision Department announces that the banking system will further extend and expand the comprehensive framework for deferring loan payments"

for September indicate that since the beginning of the crisis, a total of about NIS 160 billion was deferred in all segments. In this context, deferred household credit accounted for about 78 percent of total deferred credit, with housing credit accounting for 65 percent of total deferrals. As of September, payments were resumed on almost 54 percent of total loans that had been deferred (Figure 20). In the consumer segment, this rate is lower than the average and stands at about 47 percent, while in the small and midsize business sector the rate was higher than the average (payments were resumed on about 60–70 percent of the debt). Housing credit in deferral is the highest among the various segments, at about 12 percent, a rate higher than the average for the portfolio (about 7 percent). In addition, the period of deferral for about 55 percent of the total loans is expected to end by January 2020.

Figure 20
Loans for which Payment was Resumed as a Share of Loans with Deferred Payment



SOURCE: Based on published financial statements and reports to the Banking Supervision Department.

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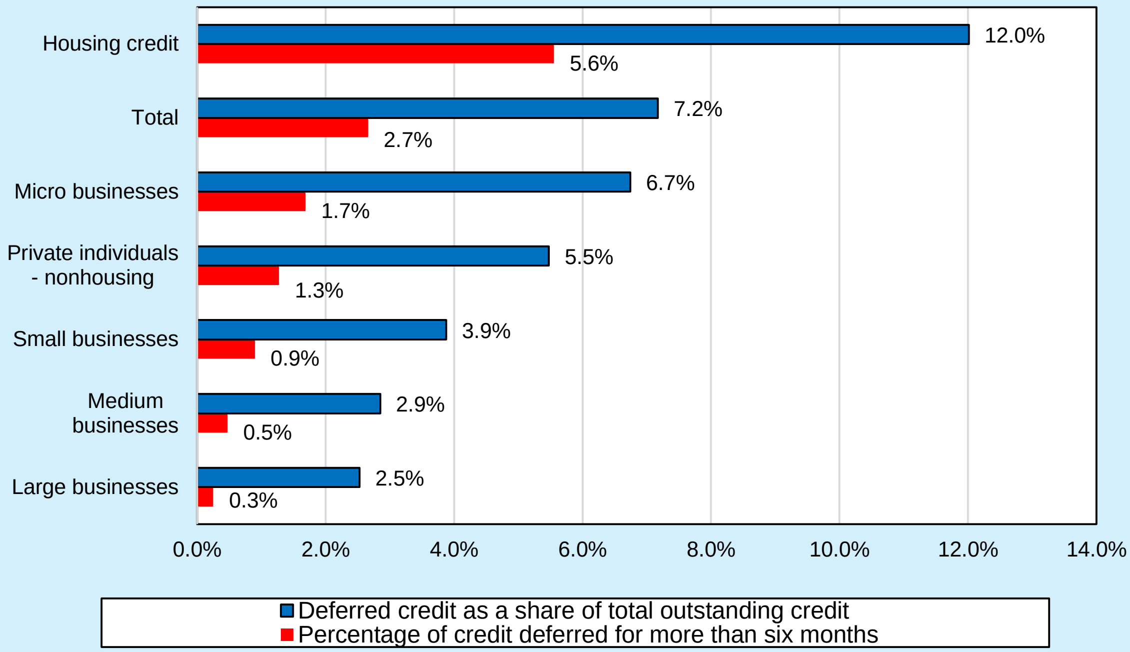
https://www.boi.org.il/en/NewsAndPublications/PressReleases/Pages/29-9-20.aspx

Figure 21
Deferred Payment Loans as a Share of Total Outstanding Credit[a], Total Banking System, September 2020



[a] Total outstanding credit to the business sector and consumer credit are up-to-date as of June 2020. Outstanding housing credit is up-to-date as of September 2020.

SOURCE: Based on published financial statements and reports to the Banking Supervision Department.

Liquidity risk

The liquidity coverage ratio (LCR)[10] of the banks continued to rise during 2020, and as a result it continued to exceed the minimum requirement established by the Banking Supervision Department (100 percent). The liquidity quality profile of the Israeli banks is determined by the regulatory steps taken by the Banking Supervision Department to improve the

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[10] The LCR, developed by the Basel Committee to enhance the short-term resilience of banking corporations' liquidity profiles, is a measure of the quantity of High-Quality Liquid Assets (HQLA) that corporations should hold in order to withstand a significant stress scenario that lasts thirty calendar days. The LCR is composed of two elements. The first, on the numerator side, is the inventory of HQLA, comprised of two levels of assets: Level 1, formed of high-quality assets that may be held in unlimited amounts, and Level 2, composed of assets that are limited to a maximum aggregate holding of 40 percent of the HQLA inventory. (This level is divided into two sublevels: 2A and 2B. At the latter level, the share of assets that may be held is limited to 15 percent.) The second element, on the denominator side, is the total net cash outflow, i.e., the expected total cash outflow less the expected total cash inflow in the stress scenario. The expected total cash outflow is calculated by multiplying the balances of different categories or types of balance-sheet and off-balance-sheet liabilities by their expected runoff or drawdown rates. The total expected cash inflow is calculated by multiplying outstanding contractual receivables by the rates at which they are expected to be received in the scenario, up to a cumulative 75 percent of the predicted total cash outflow.

banks' resilience to various types of shocks, and which have been implemented accordingly by the banking system.

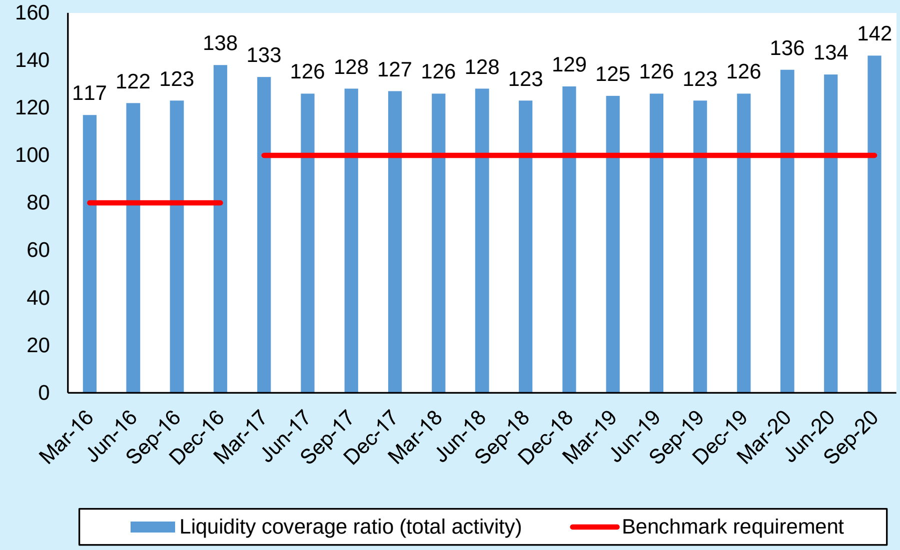
The aggregate LCR was estimated in September to be about 142 percent, which was higher than its pre-crisis level (126 percent in December 2019; Figures 21 and 22). The sharp increase in this ratio during the year is primarily the result of the large increase in the inventory of high-quality liquid assets (HQLA; an increase of 43 percent, in annual terms, since the beginning of the year). There was also a sharp increase on the net outflow side, although primarily during the second quarter of the year (Figure 24). The source of the increase in the HQLA inventory and in the net outflow is the large increase in the public's deposits.

The inventory of liquid assets grew by about NIS 119.3 billion from the beginning of 2020 until July, mainly due to the growth in cash and deposits with the Bank of Israel. The increase was made possible primarily in view of the high rate of growth in the public's deposits (about NIS 174.5 billion). **The rapid increase in the public's deposits began with the onset of the COVID-19 crisis, in view of the high volatility in the capital market. As a result of this volatility, the public shifted assets from the capital market to the banks, which are viewed as a safe haven.** Thus, by September 2020, the public's deposits had grown by 18 percent in annual terms, as compared to an annual average of about 4 percent during the three years prior to the crisis. **This development reflects the public's continuing preference for conservative channels of investment during this period, and is evidence of the public's confidence in the banking system.**

Despite the higher rate of growth in the public's deposits during the first quarter of the year, outflow grew at a faster rate during the second quarter. The reason for the differential effect on outflow during the year is related to the withdrawal coefficients of the various types of deposits. Thus, while in the first quarter of the year the growth in the public's deposits was primarily the result of an increase in retail deposits, which are weighted by negligible withdrawal coefficients, during the second quarter of the year, and alongside the growth in retail deposits, wholesale financial deposits for withdrawal in up to a month (which are weighted by a withdrawal coefficient of 100 percent) also grew significantly, increasing the outflow. During the third quarter of the year, the additional restrictions imposed on the economy led to an increase in volatility in the capital market, again leading to a sharp increase in retail deposits (weighted by, as mentioned, negligible withdrawal coefficients), and therefore to a more moderate increase in outflow.

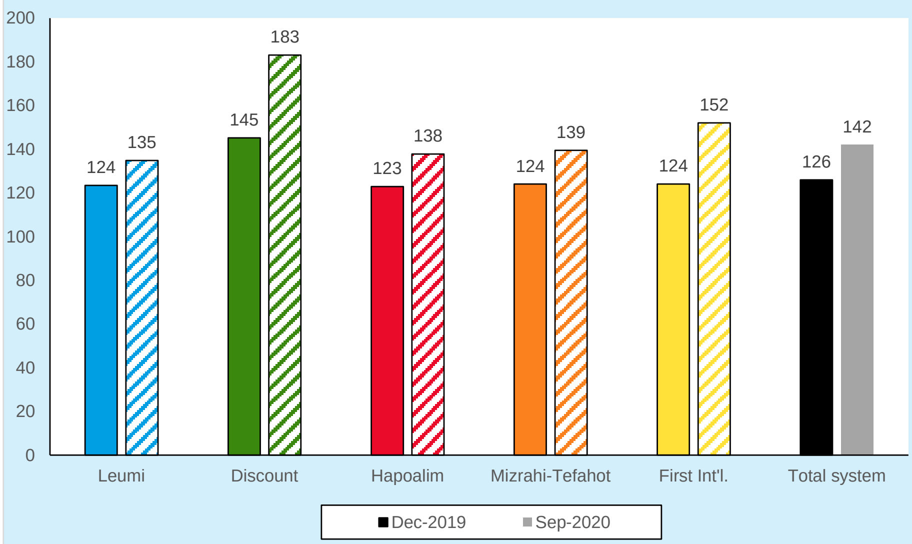
Alongside the increase in outflow, inflow declined. This was a result of both the contraction in short-term credit to the public, primarily credit to financial corporations, and the permission given by the banks to defer monthly repayments on credit (which reduced the expected inflow during the subsequent 30 calendar days).

Figure 22
Liquidity Coverage Ratio (LCR), Total Banking System, March 2016–September 2020



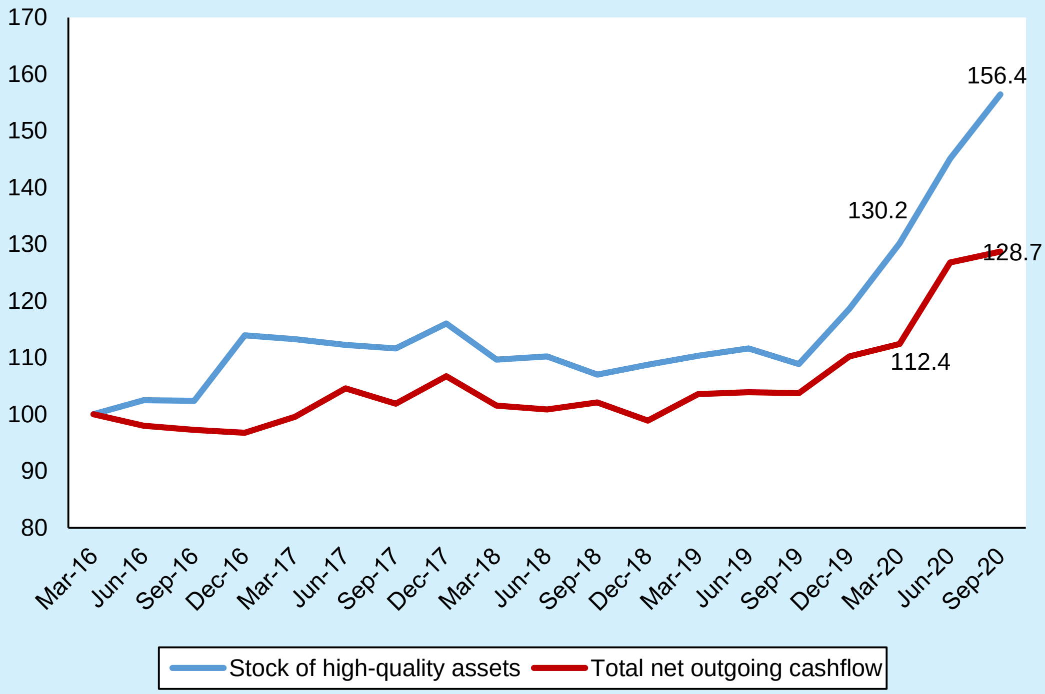
SOURCE: Based on reports to the Banking Supervision Department.

Figure 23
Liquidity Coverage Ratio (Total Activity), Total Banking System, December 2019 and September 2020



SOURCE: Based on reports to the Banking Supervision Department.

Figure 24
High-Quality Liquid Assets (HQLA)[a] and Net Outgoing Cashflow, Total Banking System, March 2016–September 2020 (Index: March 2016=100)



[a] As defined in Proper Conduct of Banking Business Directive 221.
SOURCE: Based on reports to the Banking Supervision Department.

Capital Adequacy and Leverage

As a result of the lessons learned from the Global Financial Crisis in 2008, the Banking Supervision Department has acted over the course of the last decade to strengthen the stability of the banks by improving the quality and quantity of their capital. The goal of this program was to ensure that in a realization of unexpected risks there will not be any risk to the public's deposits, and furthermore that the banking system will be resilient enough to continue supporting the economy even during the crisis. Indeed, over the course of the decade, the various steps taken by the Banking Supervision Department—which included the adoption of advanced international standards and of complementary macroprudential measures that led to an improvement in the quality and quantity of qualifying capital, the diversification of the credit portfolio, the reduction in the exposure to large borrowers and large borrower groups, and the requirement to accumulate a countercyclical sectoral capital buffer against exposure to the capital market—led to a situation in which **prior to the COVID-19 crisis, the quantity and quality of the banks' capital put them in a very favorable position in order to deal with crises, particularly the COVID-19 crisis.**

The onset of the COVID-19 virus led to a shock in the markets, which was partly reflected in a sharp increase in bond yields (Figure 13) and a drop in share prices. These shocks led to a sudden erosion of total banking capital, primarily by way of a drop in the value of ready-for-sale bonds. In parallel, business credit grew rapidly in view of the rise in the exploitation of credit lines, primarily among large businesses, which led to a rapid increase in risk assets in the banking system. These two trends led to a situation in which, already early on in the crisis, the banks' capital ratios were quickly eroded. **In response to these shocks, and from a long-term perspective of the development of the economic crisis and the credit needs of the economy, the Banking Supervision Department called on the banking system—already early on in the crisis—to utilize their capital buffers. Later on, it also decided to reduce the supervisory capital requirements[11], with the goal of ensuring that the banking system would continue to provide credit to the public and to support economic activity, despite the credit losses that it was expected to absorb.** In addition, the Banking Supervision Department instructed the heads of the banks to reexamine their dividend and share buyback policies. **As a result of this directive, the banks declared that they do not intend to distribute dividends in 2020 due to the COVID-19 crisis.**

In parallel, **the Banking Supervision Department carried out a stress test analysis of various scenarios of how the global crisis would develop, with the goal of assessing the ability of the banks in particular and the banking system in general to continue providing credit to the public, while maintaining their stability and resilience. These scenarios indicate that there is no expected risk to the stability of Israeli banks.**

In that context, **and following the relatively steep drop in the Common Equity Tier 1 Capital ratio for the system as a whole during the first quarter, the ratio recovered somewhat, to 10.9 percent as compared to 10.6 percent in March and 11.2 percent at the end of 2019 (Table 11). The improvement in the capital adequacy ratio during the second quarter of the year was due both to the slight increase in Tier 1 Equity Capital and to the slight drop in risk assets.**

Total equity in the banking system grew during the first quarter of the year by about 2.9 percent (in annual terms), to about NIS 119.9 billion. The growth in equity continued at a low rate relative to the average during the last three years (6.4 percent), which was primarily due to a low rate of profit accumulation (in view of the growth in loan loss provisions). The recovery of bond prices in the second quarter of the year led to two opposing effects on equity relative to the first quarter of the year: an increase in the fair value of ready-for-sale bonds, thus contributing to the strengthening of equity, and a drop in the discount rate used to calculate employee compensation

[11] For further details see the press releases on the reduction in capital requirements in the banking system: "The Banking Supervision Department announces a reduction in the banks' capital requirements, and instructs them to examine the distribution of dividends in order to increase the supply of credit in the economy" on March 29, 2020, and "The Banking Supervision Department is adopting further regulatory leniencies, with the aim of assisting borrowers during the crisis" on April 21, 2020.

liabilities, thus increasing those liabilities. For most of the banks in the system, the net effect of the increase in bond prices contributed to strengthening equity in the second quarter.[12]

As a result, **total Common Equity Tier 1 Capital in the system grew during the second quarter to about NIS 121 billion (Table 11).** As a result of this increase, Common Equity Tier 1 Capital grew by about 0.6 percent (in annual terms) relative to the end of 2019, which followed a significant contraction in the first quarter.

The slowdown in economic activity in the second quarter of the year, which was partly reflected in the contraction of total credit to the public (for further discussion, see the section on credit), led to a situation in which the risk declined of the five large banks fell in that quarter. Nonetheless, total risk assets in the banking system increased by 5.9 percent relative to the end of 2019, due to the fact that the drop in the second quarter occurred after a sharp increase in risk assets in the first quarter (by 13.4 percent), in view of the rapid growth in credit to large businesses.

The total capital ratio also improved relative to the first quarter of the year and stood at 14.3 percent, as opposed to 14 percent in the first quarter and 14.66 percent at the end of 2019.

On the other hand, the leverage ratio[13] continued to erode in the second quarter of the year, despite the increase in Common Equity Tier 1 Capital. **This was due to the sharp increase in the system's total exposure** (an increase of 15.3 percent in the first half of the year, in annual terms, as compared to an average annual increase of 2.9 percent in the last three years). The leverage ratio obligates the banks to put aside a minimum level of capital, determined by the volume of their activity, independently of their risk characteristics. It therefore differs from the risk-based capital ratios. With the onset of the COVID-19 crisis, there was a sharp rise in the public's deposits, which on the uses side led to an increase in cash and deposits at the Bank of Israel. Although this exposure did not bring about an increase in risk assets (since it is not accompanied by risk to the banking system and therefore it has a risk weight of zero), it did lead to the same significant increase in the banks' total exposure. Thus, **the leverage ratio reached 6.4 percent in June of this year, as compared to 6.9 percent in December 2019 (Table 9).** In view of the continuing downward trend in this ratio, **the Banking Supervision Department announced a reduction in the leverage ratio requirements on the banking system.** In this context, it was decided, by means of a temporary directive, to reduce the requirement to a minimum ratio of 5.5 percent for the large banks (as opposed to 6 percent) and to 4.5 percent for the midsize and small banks (as opposed to 5 percent).[14]

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[12] For Bank Leumi, the increase in employee compensation liabilities was particularly large and even led to a drop in equity relative to the first quarter. Nonetheless, and in contrast to equity, Bank Leumi's Common Equity Tier 1 Capital grew during the quarter, thanks to the supervisory leniency in the method of calculating the discount rate for employee compensation liabilities. According to this leniency, the discount rate for calculating the bank's obligations to its workers is calculated according to an average of the market yields over eight quarters. Therefore, in the second quarter the discount rate increased relative to the previous one, which reduced the employee compensation liabilities.

[13] Calculated as the ratio of Common Equity Tier 1 Capital to total exposures, according to the Basel III rules.

[14] See the press release on November 1st, 2020.

Balance-Sheet Activity

The aggregate balance sheet of the five largest banks grew during the first half of the year by a particularly high rate of about 17 percent (in annual terms[15]), to about NIS 1,804 billion (Table 7). The growth in the balance sheet occurred in view of a significant increase in the public's deposits (about 21 percent) as a result of the shift of funds from the capital market, following the increase in volatility in the capital markets due to the COVID-19 virus. The trend in the balance sheet was hardly affected by the shekel's appreciation against the dollar (about 0.3 percent), such that even after adjusting for the effect of the exchange rate the balance sheet of the five large banks grew by about 16.9 percent.

On the assets side, there was a significant increase during the first half of the year in both the quantity of cash and deposits with the Bank of Israel (60 percent) and in the securities portfolio (about 21 percent), which led to an increase in their share of total assets to about 34 percent as opposed to about 30 percent in December 2019. In addition, credit to the public grew during the reviewed period by about 34 percent. This increase on the assets side was made possible by the significant increase in the public's deposits on the sources side (about 21 percent), due the unprecedented shift of funds at the beginning of the crisis from the capital market to the safe haven of deposits in the banking system, in view of the increased uncertainty and volatility in the markets. The increase in the public's deposits was partly due to the significant growth in deposits by retailers and small businesses (which explains about 65 percent of the increase). With respect to changes in the volume of deposits by size, the growth was primarily due to an increase in deposits of up to NIS 10 million (which explains about 84 percent of the increase). Apart from that, the trend in capital accumulation continued in most of the banks (about 3 percent; for further discussion, see the section on capital and capital adequacy).

[15] All of the data in this section are presented in annual terms.

Table 1

Structure of the banking system, June 2020[a]

Bank	Share of total banking system assets	Share of total bank credit	Total assets	Credit to the public	Total deposits	Equity
	Balance-sheet data					
	(Percent)		(NIS million)			
Bank Leumi LeIsrael	28.7	25.8	517,650,000	289,048,000	416,956,000	36,593,000
Bank Hapoalim	27.7	26.8	499,280,000	299,690,000	400,816,000	38,054,000
Israel Discount Bank	15.6	16.7	282,100,000	186,841,000	222,048,000	19,523,000
Bank Mizrahi-Tefahot	16.2	19.4	291,560,000	216,538,000	231,784,000	17,470,000
First International Bank of Israel	8.5	8.1	152,719,000	90,371,000	129,160,000	9,085,000
Total for the five banking groups	**96.6**	**96.7**	**1,743,309,000**	**1,082,488,000**	**1,400,764,000**	**120,725,000**
Union Bank of Israel	2.5	2.3	45,712,000	25,236,000	35,607,000	2,532,000
Bank of Jerusalem	0.8	1.0	15,082,000	11,214,500	11,979,600	977,500
Total for the independent banks	**3.4**	**3.3**	**60,794,000**	**36,450,500**	**47,586,600**	**3,509,500**
Total for banking system	**100**	**100**	**1,804,123,880**	**1,118,943,699**	**1,448,368,385**	**124,234,500**

[a] Financial data for the five banking groups are presented on a conslidated basis.

SOURCE: Banking Supervision Department based on published financial statements.

Table 2

Main items in consolidated profit and loss statements of the five banking groups, June 2019, December 2019, and June 2020

(NIS millon, at current prices)

	Leumi				Hapoalim				Discount			
	Dec-19	Jun-19	Jun-20	% change June 2020 compared with June 2019	Dec-19	Jun-19	Jun-20	% change June 2020 compared with June 2019	Dec-19	Jun-19	Jun-20	% change June 2020 compared with June 2019
Interest income	11,437	6,235	5,091	-18.3	11,920	6,555	5,074	-22.6	7,567	3,956	3,533	-10.7
Interest expenses	2,596	1,649	801	-51.4	2,601	1,812	716	-60.5	1,674	940	615	-34.6
Net interest income	**8,841**	**4,586**	**4,290**	**-6.5**	**9,319**	**4,743**	**4,358**	**-8.1**	**5,893**	**3,016**	**2,918**	**-3.2**
Loan loss provisions	609	270	1,735	542.6	1,276	440	1,937	340.2	690	277	1,188	328.9
Net interest income after loan loss provisio	**8,232**	**4,316**	**2,555**	**-40.8**	**8,043**	**4,303**	**2,421**	**-43.7**	**5,203**	**2,739**	**1,730**	**-36.8**
Noninterest income	**5,081**	**2,749**	**1,727**	**-37.2**	**3,889**	**1,891**	**2,179**	**15.2**	**3,771**	**1,850**	**2,090**	**13.0**
of which: Noninterest financing income	1,686	998	30	-97.0	559	255	499	95.7	742	402	693	72.4
of which: Stocks[a]	475	506	-81	-116.0	297	250	-93	-137.2	123	81	-1	-101.2
Bonds[b]	339	97	287	195.9	225	53	122	130.2	158	83	368	343.4
Activity in derivative instruments[c]	-1,112	-867	275	-131.7	-1,260	-903	664	-173.5	-846	-556	112	-120.1
Exchange rate differentials	1,969	1,262	-451	-135.7	1,288	854	-194	-122.7	1,300	787	214	-72.8
of which: Fees	3,225	1,626	1,669	2.6	3,240	1,589	1,609	1.3	2,972	1,439	1,389	-3.5
Total operating and other expenses	**7,908**	**3,896**	**3,472**	**-10.9**	**8,776**	**3,869**	**3,742**	**-3.3**	**6,299**	**3,100**	**3,114**	**0.5**
of which: salaries and related expenses	4,325	2,261	1,846	-18.4	4,108	2,086	1,925	-7.7	3,343	1,704	1,618	-5.0
Pre-tax profit	**5,405**	**3,169**	**810**	**-74.4**	**3,156**	**2,325**	**858**	**-63.1**	**2,675**	**1,489**	**706**	**-52.6**
Provision for tax on profits	1,830	1,120	320	-71.4	1,681	890	436	-51.0	932	524	256	-51.1
After tax profit	**3,575**	**2,049**	**490**	**-76.1**	**1,475**	**1,435**	**422**	**-70.6**	**1,743**	**965**	**450**	**-53.4**
Net profit attributed to shareholders	**3,522**	**2,015**	**462**	**-77.1**	**1,799**	**1,692**	**325**	**-80.8**	**1,702**	**950**	**453**	**-52.3**
Capital for calculating ROE			35,538				28,304				18,875	
Total after-tax ROE (percent)	**9.80**	**11.40**	**2.60**		**3.86**	**7.70**	**2.30**		**9.40**	**11.10**	**4.80**	
Total ROA (percent)	**0.76**	**0.87**	**0.19**		**0.39**	**0.74**	**0.13**		**0.68**	**0.79**	**0.33**	

	Mizrahi-Tefahot				First International				The five groups			
	Dec-19	Jun-19	Jun-20	% change June 2020 compared with June 2019	Dec-19	Jun-19	Jun-20	% change June 2020 compared with June 2019	Dec-19	Jun-19	Jun-20	% change June 2020 compared with June 2019
Interest income	7,711	4,333	3,426	-20.9	3,085	1,638	1,429	-12.8	41,720	22,717	18,553	-18.3
Interest expenses	2,371	1,559	756	-51.5	483	338	111	-67.2	9,725	6,298	2,999	-52.4
Net interest income	**5,340**	**2,774**	**2,670**	**-3.7**	**2,602**	**1,300**	**1,318**	**1.4**	**31,995**	**16,419**	**15,554**	**-5.3**
Loan loss provisions	364	175	615	251.4	138	59	322	445.8	3,077	1,221	5,797	374.8
Net interest income after loan loss provisio	**4,976**	**2,599**	**2,055**	**-20.9**	**2,464**	**1,241**	**996**	**-19.7**	**28,918**	**15,198**	**9,757**	**-35.8**
Noninterest income	**1,966**	**950**	**1,068**	**12.4**	**1,520**	**749**	**754**	**0.7**	**16,227**	**8,189**	**7,818**	**-4.5**
of which: Noninterest financing income	357	146	140	-4.1	225	112	61	-45.5	3,569	1,913	1,423	-25.6
of which: Stocks[a]	58	33	-17	-151.5	71	22	-44	-300.0	1,024	892	-236	-126.5
Bonds[b]	46	14	111	692.9	12	9	11	22.2	780	256	899	251.2
Activity in derivative instruments[c]	-1,014	-620	566	-191.3	-419	-250	-2	-99.2	-4,651	-3,196	1,615	-150.5
Exchange rate differentials	1,267	719	-520	-172.3	561	331	96	-71.0	6,385	3,953	-855	-121.6
of which: Fees	1,535	756	800	5.8	1,286	635	691	8.8	12,258	6,045	6,158	1.9
Total operating and other expenses	**3,988**	**1,997**	**1,967**	**-1.5**	**2,654**	**1,351**	**1,254**	**-7.2**	**29,625**	**14,213**	**13,549**	**-4.7**
of which: salaries and related expenses	2,562	1,284	1,240	-3.4	1,601	821	752	-8.4	15,939	8,156	7,381	-9.5
Pre-tax profit	**2,954**	**1,552**	**1,156**	**-25.5**	**1,330**	**639**	**496**	**-22.4**	**15,520**	**9,174**	**4,026**	**-56.1**
Provision for tax on profits	1,029	531	396	-25.4	478	238	145	-39.1	5,950	3,303	1,553	-53.0
After tax profit	**1,925**	**1,021**	**760**	**-25.6**	**852**	**401**	**351**	**-12.5**	**9,570**	**5,871**	**2,473**	**-57.9**
Net profit attributed to shareholders	**1,842**	**980**	**717**	**-26.8**	**865**	**407**	**339**	**-16.7**	**9,730**	**6,044**	**2,296**	**-62.0**
Capital for calculating ROE							8,370				17,134	
Total after-tax ROE (percent)	**11.90**	**13.30**	**9.00**		**10.50**	**10.20**	**8.10**		**45.46**	**53.70**	**26.80**	
Total ROA (percent)	**0.69**	**0.75**	**0.51**		**0.63**	**0.60**	**0.46**		**0.62**	**0.78**	**0.27**	

[a] Includes the profits/losses from investments in shares available for sale, profits from the sales of shares of affiliated companies, dividends and profits/losses from adjustments to fair value of tradable shares.

[b] Includes the profits/losses from investments in bonds held to maturity and available for sale and income/expenses realized and not yet realized from adjustments to fair value of tradable bonds.

[c] Includes derivative instruments not intended for hedging purposes (ALM instruments) and other derivative instruments.

SOURCE: Based on published financial statements.

Table 3

The effect of quantity[a] and price[b] on interest income and expenses, Israel and abroad, the five banking groups, June 2019 to June 2020

(change compared with the same period the previous year, NIS million)

	Quantity effect			Price effect			Net change		
	Assets side	Liabilities side	Net	Assets side	Liabilities side	Net	Assets side	Liabilities side	Contribution to net interest income
June 2020									
Credit to the public / deposits of the public in Israel	836	111	725	-3,944	-1,692	-2,252	-3,108	-1,581	-1,527
Credit to the public / deposits of the public abroad	-55	0	-55	-332	-245	-87	-387	-245	-142
Total credit to the public / deposits of the public	**781**	**111**	**670**	**-4,276**	**-1,937**	**-2,339**	**-3,495**	**-1,826**	**-1,669**
Other interest-bearing assets / liabilities in Israel	216	75	141	-777	-1,527	750	-561	-1,452	891
Other interest-bearing assets / liabilities abroad	4	-8	12	-202	-15	-187	-198	-23	-175
Total other interest-bearing assets / liabilities	**220**	**67**	**153**	**-979**	**-1,542**	**563**	**-759**	**-1,475**	**716**
Total interest income / expenses	**1,001**	**178**	**823**	**-5,255**	**-3,479**	**-1,776**	**-4,254**	**-3,301**	**-953**
June 2019									
Credit to the public / deposits of the public in Israel	930	141	789	603	770	-167	1,533	911	622
Credit to the public / deposits of the public abroad	167	49	118	148	204	-56	315	253	62
Total credit to the public / deposits of the public	**1,097**	**190**	**907**	**751**	**974**	**-223**	**1,848**	**1,164**	**684**
Other interest-bearing assets / liabilities in Israel	15	96	-81	692	203	489	707	299	408
Other interest-bearing assets / liabilities abroad	23	-10	33	90	-17	107	113	-27	140
Total other interest-bearing assets / liabilities	**38**	**86**	**-48**	**782**	**186**	**596**	**820**	**272**	**548**
Total interest income / expenses	**1,135**	**276**	**859**	**1,533**	**1,160**	**373**	**2,668**	**1,436**	**1,232**
December 2019									
Credit to the public / deposits of the public in Israel	1,479	222	1,257	-1,492	280	-1,772	-13	502	-515
Credit to the public / deposits of the public abroad	132	58	74	87	199	-112	219	257	-38
Total credit to the public / deposits of the public	**1,611**	**280**	**1,331**	**-1,405**	**479**	**-1,884**	**206**	**759**	**-553**
Other interest-bearing assets / liabilities in Israel	67	75	-8	735	-727	1,462	802	-652	1,454
Other interest-bearing assets / liabilities abroad	-35	-26	-9	77	-58	135	42	-84	126
Total other interest-bearing assets / liabilities	**32**	**49**	**-17**	**812**	**-785**	**1,597**	**844**	**-736**	**1,580**
Total interest income / expenses	**1,643**	**329**	**1,314**	**-593**	**-306**	**-287**	**1,050**	**23**	**1,027**

[a] The quantity effect is calculated as the change in the balance-sheet balance (current year versus previous year) multiplied by the price during the current period, divided by 1000.

[b] The price effect is calculated as the change in price (current year versus previous year) multiplied by the balance-sheet balance for the same period in the previous year, divided by 1000.

SOURCE: Banking Supervision Department based on published financial statements.

Table 4

Average balances, financing income and expense rates, and financing rate gap in respect of assets and liabilities, the five banking groups, June 2019 to June 2020 (NIS million, percent, in annual terms)

June 2020

Assets	Average yearly balance (NIS million)	Financing income	Income rate (%)	Liabilities	Average yearly balance (NIS million)	Financing expenses	Expense rate (%)	Financing rate gap
Credit to the public	1,037,970	16,811	**3.27**	Deposits of the public	904,289	-2,393	-0.53	2.74
Deposits at banks	27,241	123	**0.91**	Deposits from banks	18,169	-530	-5.75	-4.84
Deposits at central banks	239,271	242	**0.20**	Deposits from central banks	1,479	-53	-7.04	-6.84
Bonds	207,004	1,261	**1.22**	Bonds	94,834	-530	-1.11	0.11
Other assets[a]	15,509	116	1.50	Other liabilities[a]	5,672	-21	-0.74	0.76
Total interest-bearing assets	1,526,995	18,553	2.44	Total interest-bearing liabilities	1,024,443	-2,999	-0.58	1.86
Net yield on interest-bearing assets (net interest margin)[b]	1,526,995	15,554	2.05					

June 2019

Assets	Average yearly balance (NIS million)	Financing income	Income rate (%)	Liabilities	Average yearly balance (NIS million)	Financing expenses	Expense rate (%)	Financing rate gap
Credit to the public	988,047	20,306	4.15	Deposits of the public	857,528	-4,219	-0.99	3.16
Deposits at banks	22,195	207	1.88	Deposits from banks	15,626	-1,978	-0.82	1.06
Deposits at central banks	189,687	431	0.84	Deposits from central banks	597	-64	-2.36	-1.52
Bonds	197,384	1,728	**1.76**	Bonds	91,160	-1,978	**-4.39**	-2.63
Other assets[a]	12,681	135	2.14	Other liabilities[a]	3,698	-32	-1.72	0.42
Total interest-bearing assets	1,409,994	22,807	3.26	Total interest-bearing liabilities	968,609	-6,300	-1.31	1.95
Net yield on interest-bearing assets (net interest margin)[b]	1,409,994	16,507	2.36					

December 2018

Assets	Average yearly balance (NIS million)	Financing income	Income rate (%)	Liabilities	Average yearly balance (NIS million)	Financing expenses	Expense rate (%)	Financing rate gap
Credit to the public	995,541	37,269	3.74	Deposits of the public	856,313	-7,131	-0.83	2.91
Deposits at banks	23,372	384	1.64	Deposits from banks	15,808	-123	-0.78	0.86
Deposits at central banks	185,769	788	0.42	Deposits from central banks	405	-10	-2.47	-2.05
Bonds	198,527	3,109	1.57	Bonds	92,029	-2,408	-2.62	-1.05
Other assets[a]	12,401	248	2.00	Other liabilities[a]	3,795	-57	-1.50	0.50
Total interest-bearing assets	1,415,610	41,798	2.96	Total interest-bearing liabilities	968,350	-9,729	-1.00	1.96
Net yield on interest-bearing assets (net interest margin)[b]	1,415,610	32,069	2.27					

[a] Other liabilities and assets also include credit to the government and government deposits, and securities loaned or borrowed in repurchase agreements, among other things.

[b] The net interest margin is the ratio between net interest income and total interest-bearing assets. The margin is shown in percent.

SOURCE: Banking Supervision Department based on published financial statements.

Table 5

Outstanding credit to the public, by principal industries, the five banking groups, December 2019 and June 2020

	Total balance of credit risk[a]					Balance-sheet credit[b] (debts)				
	Balance		Distribution of credit to the public		Change in credit[c]	Balance		Distribution of credit to the public		Change in credit[c]
	Dec-19	Jun-20	Dec-19	Jun-20	Jun-20	Dec-19	Jun-20	Dec-19	Jun-20	Jun-20
	(NIS million)		(percent)		(percent)	(NIS million)		(percent)		(percent)
Total borrowers' activi	**1,387,714**	**1,429,343**	**90.2**	**90.1**	**6.0**	**979,761**	**998,589**	**92.3**	**92.2**	**3.8**
Business	**749,932**	**778,667**	**48.7**	**49.1**	**7.7**	**467,551**	**478,582**	**44.0**	**44.2**	**4.7**
Construction and real est	195,008	201,206	12.7	12.7	6.4	84,846	89,909	8.0	8.3	11.9
Construction and real est	78,822	82,370	5.1	5.2	9.0	67,626	70,906	6.4	6.6	9.7
Financial services	110,013	115,399	7.2	7.3	9.8	57,794	53,243	5.4	4.9	-15.7
Other Business	366,089	379,692	23.8	23.9	7.4	257,285	264,524	24.2	24.4	5.6
Private individuals	**637,782**	**650,676**	**41.5**	**41.0**	**4.0**	**512,210**	**520,007**	**48.2**	**48.0**	**3.0**
Private individuals - hous	400,637	418,067	26.0	26.4	8.7	371,203	387,247	35.0	35.8	8.6
Private individuals - other	237,145	232,609	15.4	14.7	-3.8	141,007	132,760	13.3	12.3	-11.7
Total borrowers' activi	**150,637**	**156,768**	**9.8**	**9.9**	**8.1**	**81,913**	**83,899**	**7.7**	**7.8**	**4.8**
Total	**1,538,351**	**1,586,111**	**100.0**	**100.0**	**6.2**	**1,061,674**	**1,082,488**	**100.0**	**100.0**	**3.9**

[a] Includes balance-sheet and non-balance-sheet credit risk.

[b] Includes credit to the public, excludes bonds and securities borrowed or purchased under reverse repurchase agreements.

[c] In annual terms.

SOURCE: Banking Supervision Department based on published financial statements.

Table 6

Unit output cost[a] and efficiency ratio[b] of the banking corporations in Israel, December 2018 to June 2020

(percent)

	Unit output cost				Efficiency ratio			
Bank	Dec-18	Dec-19	Jun-19	Jun-20	Dec-18	Dec-19	Jun-19	Jun-20
Leumi	1.83	1.70	1.68	1.41	60.6	56.8	53.1	57.7
Hapoalim	1.96	1.90	1.69	1.55	65.1	66.4	58.3	57.2
Discount	2.67	2.52	2.56	2.30	68.2	65.2	63.7	62.2
Mizrahi-Tefahot	1.76	1.50	1.53	1.39	63.6	54.6	53.6	52.6
First International	2.09	1.93	2.01	1.71	68.4	64.4	65.9	60.5
Five banking groups	**2.01**	**1.88**	**1.82**	**1.62**	**64.4**	**61.4**	**57.8**	**58.0**
Union	2.25	2.04	2.07	1.92	81.1	74.8	77.0	87.8
Jerusalem	3.01	2.97	2.87	2.67	72.4	70.0	70.4	63.2
Total banking system	**2.02**	**1.89**	**1.84**	**1.63**	**64.9**	**61.8**	**58.3**	**58.6**

[a] The ratio between total operating and other expenses and the average balance of assets (average cost).

[b] The ratio between total operating and other expenses and total net interest and noninterest income (cost-to-income)

SOURCE: Based on published financial statements.

Table 7
Indices of credit portfolio quality of the five banking groups, 2015 to June 2020
(percent)

	Year	Leumi	Hapoalim	Discount	Mizrahi-Tefahot	First International	The five groups
Annual loan loss provision as a share of total balance-sheet credit to the public[a]	2015	0.08	0.18	0.15	0.13	0.02	0.12
	2016	-0.05	0.07	0.33	0.12	0.10	0.09
	2017	0.06	0.07	0.38	0.11	0.15	0.13
	2018	0.18	0.21	0.32	0.16	0.19	0.21
	2019	0.21	0.43	0.38	0.18	0.16	0.29
	June-20[b]	1.20	1.29	1.26	0.57	0.71	1.07
Net write-offs as a share of total balance-sheet credit to the public	2015	0.20	0.08	0.12	0.09	0.14	0.13
	2016	0.03	0.19	0.27	0.09	0.09	0.13
	2017	0.15	0.21	0.39	0.09	0.17	0.19
	2018	0.09	0.19	0.25	0.11	0.16	0.15
	2019	0.23	0.12	0.22	0.11	0.09	0.16
	June-20[b]	0.27	0.29	0.24	0.16	0.18	0.24
Allowance for credit losses as a share of total balance-sheet credit to the public	2015	1.38	1.58	1.59	0.87	1.12	1.36
	2016	1.32	1.50	1.50	0.83	1.08	1.29
	2017	1.18	1.36	1.40	0.81	1.03	1.18
	2018	1.24	1.31	1.36	0.80	1.02	1.18
	2019	1.16	1.58	1.38	0.82	1.05	1.24
	June-20	1.60	2.00	1.82	0.96	1.28	1.60
Problematic loans as a share of total balance-sheet credit to the public	2015	3.14	3.57	3.54	1.38	2.39	2.95
	2016	2.90	2.89	3.55	1.44	2.29	2.67
	2017	2.71	2.37	2.80	1.39	1.78	2.30
	2018	2.45	2.30	2.23	1.52	1.89	2.15
	2019	1.96	3.06	2.56	1.78	1.86	2.33
	June-20	2.18	3.08	2.85	1.80	1.97	2.45
Impaired loans and non-impaired loans 90 days or more past due as a share of total balance-sheet credit to the public	2015	1.83	2.28	2.60	1.14	1.36	1.92
	2016	1.75	1.84	2.37	0.95	1.02	1.66
	2017	1.60	1.31	1.68	1.02	0.92	1.36
	2018	1.34	1.23	1.24	1.23	0.83	1.23
	2019	1.23	1.80	1.25	1.36	1.08	1.41
	June-20	1.28	1.70	1.37	1.34	1.18	1.41
Allowance for credit losses as a share of impaired loans and non-impaired loans more than 90 days past due	2015	75.49	69.19	61.14	76.54	82.57	70.96
	2016	75.02	81.56	63.38	87.74	106.14	77.50
	2017	74.02	103.16	83.21	79.83	112.18	86.75
	2018	92.17	106.49	109.96	65.16	122.25	95.63
	2019	94.79	87.90	110.12	60.23	97.08	88.31
	June-20	125.45	117.40	133.16	72.22	108.85	112.85
Impaired loans and non-impaired loans 90 days or more past due, net, as a share of total equity	2015	4.10	5.74	9.56	3.46	2.37	5.23
	2016	3.67	2.62	8.30	1.51	-0.64	3.39
	2017	3.36	-0.31	2.65	2.62	-1.13	1.60
	2018	0.83	-0.61	-1.17	5.47	-1.88	0.48
	2019	0.51	1.70	-1.21	6.65	0.31	1.47
	June-20	-2.57	-2.33	-4.34	4.60	-1.03	-1.63

[a] Until December 2010, net credit to the public was used. From 2011, gross credit to the public.

[b] In annual terms.

SOURCE: Based on published financial statements.

Table 8

Credit quality[a] by principal segments, the five banking groups, December 2013–June 2020

(percent)

	Year	Leumi	Hapoalim	Discount	Mizrahi-Tefahot	First International	The five groups
Commercial credit							
Weight of commercial credit	2013	58.21	60.97	66.08	25.67	53.31	54.27
	2014	56.63	60.10	65.51	25.28	51.37	53.14
	2015	54.81	59.38	64.57	23.94	49.67	51.76
	2016	55.66	57.88	62.84	23.12	49.24	50.87
	2017	57.70	58.89	61.81	23.55	47.94	51.33
	2018	59.01	56.52	61.94	25.10	47.04	51.27
	2019	60.65	56.86	61.23	24.34	46.81	51.47
	June-20	60.76	56.60	61.75	26.07	46.81	51.67
Loan loss provisions as a share of total commercial credit	2013	0.02	0.41	0.69	0.11	0.12	0.29
	2014	0.06	0.09	0.04	0.22	-0.04	0.07
	2015	-0.08	0.17	0.14	0.39	-0.07	0.09
	2016	-0.39	-0.14	0.28	0.24	0.08	-0.09
	2017	-0.01	-0.21	0.26	0.11	0.15	0.00
	2018	0.15	0.07	0.17	0.33	0.25	0.16
	2019	0.26	0.62	0.31	0.44	0.16	0.39
	June-20	1.54	1.51	1.31	1.46	1.09	1.44
Impaired credit as a share of total commercial credit	2013	3.91	4.52	4.81	3.22	2.30	4.09
	2014	3.18	3.47	3.36	1.87	1.87	3.11
	2015	2.62	2.76	3.45	1.85	1.86	2.70
	2016	2.37	2.02	3.21	1.46	1.26	2.24
	2017	1.95	1.18	2.19	1.44	1.15	1.64
	2018	1.42	1.25	1.43	1.96	0.92	1.38
	2019	1.28	2.17	1.45	2.25	1.33	1.69
	June-20	1.25	2.04	1.59	2.18	1.40	1.67
Loan loss allowance as a share of total impaired commercial credit	2013	52.55	40.71	41.52	46.02	63.54	45.86
	2014	62.06	52.33	52.41	76.60	79.82	57.99
	2015	66.47	69.63	52.26	84.69	73.34	65.79
	2016	63.89	88.97	53.47	107.19	103.09	72.82
	2017	67.63	125.88	68.81	99.68	105.37	86.11
	2018	95.34	122.33	100.20	70.33	133.24	102.47
	2019	100.18	95.43	101.72	66.70	98.55	94.34
	June-20	147.30	125.53	123.70	81.74	119.26	124.12

Table 8 cont'd.

Credit quality[a] by principal segments, the five banking groups, December 2013–June 2020

(percent)

	Year	Leumi	Hapoalim	Discount	Mizrahi-Tefahot	First International	The five groups
Housing credit							
Weight of housing credit	2013	28.51	21.09	16.96	64.39	24.93	30.34
	2014	29.58	21.08	16.70	64.63	26.15	30.88
	2015	30.86	21.60	16.87	65.97	27.30	31.90
	2016	29.81	22.36	18.03	66.55	27.81	32.43
	2017	28.75	24.18	19.15	66.02	28.13	33.02
	2018	28.47	28.41	19.71	64.83	28.56	34.02
	2019	29.54	30.14	20.31	65.69	28.80	35.08
	June-20	30.04	31.54	21.25	64.94	29.63	35.89
Loan loss provisions as a share of total housing credit	2013	0.08	0.20	0.15	0.21	0.19	0.17
	2014	0.03	-0.07	0.09	0.01	-0.02	0.00
	2015	0.02	0.01	0.02	0.01	0.01	0.01
	2016	-0.01	-0.01	0.03	0.01	0.01	0.00
	2017	-0.02	-0.02	0.05	0.02	0.00	0.00
	2018	0.04	0.04	0.07	0.03	0.02	0.04
	2019	0.03	0.03	0.07	0.03	0.01	0.03
	June-20	0.16	0.29	0.23	0.08	0.10	0.17
Impaired credit and credit 90 days or more past due as a share of total housing	2013	1.13	1.93	2.17	1.20	1.58	1.44
	2014	1.01	1.27	2.06	0.98	1.28	1.15
	2015	0.92	1.04	1.48	0.90	0.91	0.98
	2016	0.91	0.96	1.13	0.74	0.69	0.86
	2017	0.93	0.91	0.98	0.89	0.68	0.89
	2018	1.07	0.78	0.94	0.98	0.76	0.93
	2019	0.98	0.77	0.95	1.09	0.73	0.95
	June-20	1.01	0.75	0.98	1.02	0.83	0.93
Loan loss allowance as a share of total housing credit 90 days or more past due	2013	63.36	40.50	58.39	59.76	55.11	54.48
	2014	66.67	53.97	61.76	66.03	56.41	62.07
	2015	68.13	61.83	53.73	64.23	65.38	63.61
	2016	65.79	61.72	57.53	72.10	76.67	66.63
	2017	62.33	66.89	63.12	58.82	73.72	62.66
	2018	55.57	67.09	60.32	51.52	64.32	57.21
	2019	56.27	64.36	58.64	45.66	65.05	54.13
	June-20	68.60	100.99	75.26	54.68	67.87	70.11

Table 8 cont'd.

Credit quality[a] by principal segments, the five banking groups, December 2013–June 2020

(percent)

	Year	Leumi	Hapoalim	Discount	Mizrahi-Tefahot	First International	The five groups
Other private credit							
Weight of other private credit	2013	13.28	17.93	16.96	9.94	21.76	15.39
	2014	13.79	18.82	17.79	10.09	22.48	15.98
	2015	14.33	19.01	18.56	10.09	23.03	16.34
	2016	14.53	19.76	19.13	10.32	22.94	16.70
	2017	13.55	16.93	19.04	10.44	23.93	15.66
	2018	12.52	15.07	18.35	10.08	24.40	14.72
	2019	9.81	13.00	18.46	9.98	24.39	13.45
	June-20	9.19	11.86	17.00	9.00	23.57	12.44
Loan loss provisions as a share of total other private credit	2013	0.56	0.28	0.06	0.41	0.14	0.32
	2014	1.01	0.65	0.52	0.62	0.69	0.72
	2015	0.81	0.33	0.29	0.34	0.23	0.44
	2016	1.19	0.74	0.76	0.52	0.26	0.78
	2017	0.52	1.20	1.10	0.65	0.32	0.83
	2018	0.65	1.06	1.11	0.54	0.30	0.80
	2019	0.48	0.49	0.92	0.49	0.32	0.57
	June-20	1.82	2.15	2.07	0.86	0.59	1.64
Impaired credit[b] and credit 90 days or more past due[c] as a share of total other	2013	1.04	1.83	0.80	0.72	0.80	1.22
	2014	0.79	1.53	0.63	0.63	0.78	1.02
	2015	0.62	1.46	0.52	0.61	0.63	0.91
	2016	0.73	1.54	0.55	0.54	0.69	0.96
	2017	1.34	1.86	0.57	0.49	0.58	1.14
	2018	1.31	1.90	0.72	0.51	0.60	1.16
	2019	1.32	2.23	0.75	0.53	0.79	1.24
	June-20	1.61	2.41	0.78	0.60	0.85	1.36
Loan loss allowance as a share of total impaired other private credit and private credit 90 days or more past due[c]	2013	135.21	77.95	202.50	137.00	110.74	109.50
	2014	215.30	112.31	275.91	190.43	172.13	159.25
	2015	267.52	100.64	299.20	184.85	195.28	161.56
	2016	280.07	105.46	290.00	205.21	186.29	169.99
	2017	142.77	105.19	323.93	253.76	223.01	152.75
	2018	165.45	106.11	272.97	250.50	209.68	159.30
	2019	172.63	87.22	263.49	240.00	153.49	146.26
	June-20	184.11	108.51	337.50	254.70	164.84	172.07

[a] Including credit in respect of borrowers' activity in Israel and abroad.

[b] Including impaired credit to all private individuals in respect of borrowers' activity abroad.

[c] Including impaired credit and credit 90 days or more past due to all private individuals in respect of borrowers' activity abroad.

SOURCE: Banking Supervision Department based on published financial statements.

Table 9

Main capital indices of the five banking groups, December 2016 to June 2020

(percent)

	Year	Leumi	Hapoalim	Discount	Mizrahi-Tefahot	First Int'l.	Five Groups
Common Equity Tier 1 capital ratio[a]	2016	11.2	11.0	9.8	10.1	10.1	10.7
	2017	11.4	11.3	10.0	10.2	10.4	10.9
	2018	11.1	11.2	10.2	10.0	10.5	10.8
	2019	11.9	11.5	10.3	10.1	10.8	11.2
	June-20	11.5	11.2	10.1	10.0	10.7	10.9
Leverage ratio[b]	2016	6.77	7.25	6.60	5.27	5.52	6.55
	2017	6.94	7.37	6.81	5.48	5.50	6.70
	2018	7.05	7.51	6.90	5.42	5.76	6.79
	2019	7.34	7.61	6.87	5.55	5.81	6.91
	June-20	6.71	6.97	6.44	5.36	5.49	6.42
The ratio between equity and total balance sheet assets	2016	7.1	7.6	6.8	5.8	5.7	6.9
	2017	7.4	7.9	7.3	6.0	5.7	7.1
	2018	7.7	8.2	7.4	6.0	6.0	7.3
	2019	7.5	8.2	7.4	6.2	6.1	7.4
	June-20	7.0	7.6	6.9	6.0	5.7	6.9

[a] In Basel III, in accordance with the transition directives.

[b] Calculated as the ratio between Common Equity Tier 1 capital and total exposures, in accordance with the Basel III rules.

SOURCE: Based on published financial statements and reports to the Banking Supervision Department.

Table 10

Credit and spreads by supervisory activity segments, business sector[a,b], the five banking groups, December 2019 and June 2020

	Credit balances to the end of the reporting period														
	Small and micro businesses			**Medium-sized businesses**			**Large businesses**				**Total**		
	Dec-19	Jun-20	Rate of change	Dec-19	Jun-20	Rate of change	Dec-19	Jun-20	Difference	Rate of change	Dec-19	Jun-20	Rate of change
	(NIS million)		(percent)	(NIS million)		(percent)	(NIS million)			(percent)	(NIS million)		(percent)
Leumi	62,727	63,266	1.72	29,578	29,406	(1.16)	67,167	72,169	5,002	14.89	159,472	164,841	6.73
Hapoalim	54,834	54,884	0.18	29,615	31,344	11.68	67,919	67,319	-600	(1.77)	152,368	153,547	1.55
Discount	36,837	37,029	1.04	12,628	13,539	14.43	39,529	42,180	2,651	13.41	88,994	92,748	8.44
Mizrahi-Tefahot	21,241	23,079	17.31	7,196	7,413	6.03	15,357	18,417	3,060	39.85	43,794	48,909	23.36
First Int'l.	17,264	17,719	5.27	5,539	5,652	4.08	17,280	17,219	-61	(0.71)	40,083	40,590	2.53
The five groups	192,903	195,977	3.19	84,556	87,354	6.62	207,252	217,304	10,052	9.70	484,711	500,635	6.57
	Net interest margin												
	Small and micro businesses			**Medium-sized businesses**			**Large businesses**				**Total**		
	Dec-19	Jun-20	Rate of change	Dec-19	Jun-20	Rate of change	Dec-19	Jun-20	Difference	Rate of change	Dec-19	Jun-20	Rate of change
	(NIS million)		(percent)	(NIS million)		(percent)	(NIS million)			(percent)	(NIS million)		(percent)
Leumi	3.66	3.17	(13.27)	2.58	2.12	(18.09)	2.52	2.06	(0.46)	(18.43)	2.98	2.50	(16.26)
Hapoalim	4.01	3.51	(12.50)	3.10	2.83	(8.60)	2.14	2.00	(0.14)	(6.44)	3.12	2.78	(10.72)
Discount	4.11	3.69	(10.02)	3.62	3.26	(10.03)	2.49	2.35	(0.15)	(5.94)	3.42	3.11	(9.14)
Mizrahi-Tefahot	5.03	4.46	(11.45)	3.81	3.47	(8.93)	2.45	2.38	(0.07)	(2.92)	3.79	3.49	(7.86)
First Int'l.	3.57	3.38	(5.35)	3.19	2.88	(9.74)	2.06	1.88	(0.18)	(8.88)	2.96	2.73	(7.92)
The five groups	4.00	3.55	(11.33)	3.02	2.66	(11.72)	2.36	2.11	(0.25)	(10.51)	3.19	2.82	(11.59)

[a] Small and micro businesses - activity of less than NIS 50 million; Medium-sized businesses - activity of between NIS 50 million and NIS 250 million; Large businesses - activity equal to or more than NIS 250 million.

[b] The data relate to activity in Israel, and do not include institutional investors, the financial management or "others" segments, and adjustments.

SOURCE: Based on published financial statements.

Table 11

Distribution of capital and capital ratios at the five banking groups[a], December 2019 and June 2020

	Leumi		Hapoalim		Discount		Mizrahi-Tefahot		First International		The five groups	
	Dec-19	June-20	Dec-19	June-20	Dec-19	June-20	Dec-19	June-20	Dec-19	June-20	Dec-19	June-20
	(NIS million)											
Equity[b]	35,406	36,132	38,221	38,054	19,193	19,523	16,805	17,470	8,568	8,712	118,193	119,891
Common Equity Tier 1 capital[c]	37,603	37,475	38,795	38,300	19,009	19,391	16,520	17,033	8,785	8,882	120,712	121,081
Tier 1 capital[c]	0	0	733	488	534	356	0	0	0	0	1,267	844
Tier 2 capital[c]	11,987	13,735	9,707	9,730	6,021	5,296	6,090	5,966	2,345	2,741	36,150	37,468
Total capital base	49,590	51,210	49,235	48,518	25,564	25,043	22,610	22,999	11,130	11,623	158,129	159,393
Total balance sheet	469,134	517,650	463,688	499,280	259,823	282,100	273,244	291,560	141,110	152,719	1,606,999	1,743,309
Credit risk	288,340	296,428	309,303	312,747	167,372	173,714	150,878	158,555	73,862	75,685	989,755	1,017,129
Market risks	5,008	6,890	3,528	4,769	2,858	4,127	1,791	1,616	875	824	14,060	18,226
Operational risk	23,116	22,715	23,556	23,428	14,216	14,514	10,189	10,821	6,512	6,451	77,589	77,929
Total risk-weighted assets	316,464	326,033	336,387	340,944	184,446	192,355	162,858	170,992	81,249	82,960	1,081,404	1,113,284
	(Percent)											
Common Equity Tier 1 capital ratio	**11.9**	**11.5**	**11.5**	**11.2**	**10.3**	**10.1**	**10.1**	**10.0**	**10.8**	**10.7**	**11.2**	**10.9**
Tier 1 capital ratio	0.0	0.0	0.2	0.1	0.3	0.2	0.0	0.0	0.0	0.0	0.1	0.1
Tier 2 capital ratio	3.8	4.2	2.9	2.9	3.3	2.8	3.7	3.5	2.9	3.3	3.3	3.4
Total capital adequacy ratio	**15.7**	**15.7**	**14.6**	**14.2**	**13.9**	**13.0**	**13.9**	**13.5**	**13.7**	**14.0**	**14.6**	**14.3**

[a] The banking corporations allocate capital in accordance with Basel III rules, as per the transition directives.

[b] Including minority interest according to the groups' balance sheets.

[c] After deductions.

SOURCE: Based on published financial statements and reports to the Banking Supervision Department.

Table 12

Balance sheet of the total Israeli banking system[a], December 2018 to June 2020

	In current prices				Rate of change in the past 12 months	Rate of change in the first 6 months of 2020	Distribution	
	Dec-18	Jun-19	Dec-19	Jun-20			Dec-19	Jun-20
	(NIS million)				(Percent)	(Percent in annual terms)	(Percent)	
Assets								
Cash and deposits at banks	277,653	269,897	289,543	376,332	39.4	59.9	17.4	20.9
Securities	199,412	213,400	212,038	234,759	10.0	21.4	12.7	13.0
Securities borrowed or bought under reverse repurchase agreements	4,196	4,620	2,603	3,926	-15.0	101.7	0.2	0.2
Credit to the public	**1,056,290**	**1,073,417**	**1,098,524**	**1,118,939**	**4.2**	**3.7**	**66.0**	**62.0**
Allowance for credit losses	12,441	12,554	13,540	17,723	41.2	61.8	0.8	1.0
Net credit to the public	1,043,849	1,060,863	1,084,985	1,101,216	3.8	3.0	65.2	61.0
Credit to governments	7,876	7,678	7,925	8,988	17.1	26.8	0.5	0.5
Investments in subsidiary and affiliated companies	16,616	2,392	2,614	1,765	-26.2	-65.0	0.2	0.1
Premises and equipment	11,552	11,229	11,694	11,551	2.9	-2.4	0.7	0.6
Intangible assets and goodwill	503	491	515	511	4.1	-1.6	0.0	0.0
Assets in respect of derivative instruments	32,300	28,424	30,856	38,473	35.4	49.4	1.9	2.1
Other assets	20,527	21,334	20,992	26,582	24.6	53.3	1.3	1.5
Total assets	**1,614,483**	**1,620,329**	**1,663,764**	**1,804,103**	**11.3**	**16.9**	**100.0**	**100.0**
Liabilities and equity								
Deposits of the public	**1,263,523**	**1,279,489**	**1,310,331**	**1,448,351**	**13.2**	**21.1**	**78.8**	**80.3**
Deposits from banks	20,305	16,040	18,400	20,782	29.6	25.9	1.1	1.2
Deposits from governments	2,248	1,453	1,563	1,417	-2.5	-18.8	0.1	0.1
Securities lent or sold under repurchase agreements	1,667	1,509	825	1,463	-3.0	154.7	0.0	0.1
Bonds and subordinated notes	100,436	99,473	104,025	96,323	-3.2	-14.8	6.3	5.3
Liabilities in respect of derivative instruments	30,466	30,128	33,002	42,222	40.1	55.9	2.0	2.3
Other liabilities	76,548	68,992	73,002	69,312	0.5	-10.1	4.4	3.8
Total liabilities	**1,495,193**	**1,497,084**	**1,541,148**	**1,679,869**	**12.2**	**18.0**	**92.6**	**93.1**
Minority interest	2,515	2,085	2,151	2,200	5.5	4.6	0.1	0.1
Shareholders equity	116,775	121,160	120,466	122,035	0.7	2.6	7.2	6.8
Total equity	119,290	123,245	122,617	124,235	0.8	2.6	7.4	6.9
Total liabilities and equity	**1,614,483**	**1,620,329**	**1,663,764**	**1,804,103**	**11.3**	**16.9**	**100.0**	**100.0**

[a] On a consolidated basis. Includes the five banking groups (Leumi, Hapoalim, Discount, First International and Mizrahi-Tefahot), and the three independent banks (Union Bank, Bank of Jerusalem and Dexia Bank).

SOURCE: Banking Supervision Department based on published financial statements.

Box 1

Banking Supervision Department measures during the COVID-19 crisis [May to October]

Extension of the loan payments deferral program

In May 2020, the Banking Supervision Department announced a comprehensive program for the deferral of loan payments, which was adopted by the banking system and was intended to assist the banks' customers in dealing with the effects of the COVID-19 crisis.

With the goal of continuing to assist customers in dealing with their cash flow problems as a result of the crisis using informed and responsible risk management, the Banking Supervision Department announced the extension and expansion of the plan in July 2020.

The government's decision in September 2020 to impose an additional lockdown in order to deal with the COVID-19 pandemic had various effects on the banking system's customers. In order to assist these customers in coping with these effects, including a drop in income, an adverse impact on employment, and difficulty in the repayment of loans among other things, the Banking Supervision Department announced an additional expansion of the plan in September. Details of the plan appear in the Appendix.

In addition, and in order to expand the assistance to customers of the financial system as well, a voluntary plan was put together for the deferral of loan payments, which was adopted by all of the credit card companies. Details of the plan appear in the Appendix.

The formulated plan presents the minimum conditions for deferring payments on loans, and each bank or credit card company can expand them in order to better serve their customers and their needs.

The plans are intended to provide breathing space for customers who are encountering cash flow problems as a result of the persistence of the crisis and its effects. However, it should be recalled that the deferral of payments has a cost. Thus, prior to making the decision to defer payments, it is important to examine the implications of the deferral, including its economic price (the interest rate, the amount of the monthly payment following the deferral period, etc.), and to utilize this alternative only after an examination of its necessity and its cost.

Deferral of payments will not be possible for an unlimited period of time, and customers therefore need to prepare for the day after the deferral period in order to come to payment arrangements for their loans and the repayment of their debts.

In addition, the Banking Supervision Department again stressed to the banks that they should operate with sensitivity toward their customers and to avoid, to whatever extent possible, taking legal measures against customers during this challenging period. Efforts should continue to be made with the customer to reach forward-looking payment arrangements, according to the circumstances of each customer, in order to allow them to weather the continuing crisis.

<u>The Expanded Plan for the Deferral of Loan Payments by the Banking System</u>

	Customer Group	Deferral Period	Last Date for Requesting a Deferral	Method of Rescheduling the Payments	Maximum Interest Rate	Charging of Fees
Mortgages	Customers who are paying the loan on schedule, including customers whose loans were in arrears in the two months prior to the date for submitting the request. The deferral is of the principal and the interest, without the bank having any discretion.	- Customers who have already deferred their mortgage payments for a period of up to 6 months can obtain an additional deferral up to **December 31, 2020.** - Customers who have not yet deferred their mortgage payments and are now interested in doing so can obtain a deferral of **up to 6 months**, where it is possible to submit the request up to December 31, 2020.	December 31, 2020	Spread over the rest of the loan period.***	The interest rate specified in the original loan agreement.	The deferral will be carried out with no fee being charged.

Consumer credit – up to NIS 100,000 **	With respect to an additional request for deferral: a borrower not in arrears on the loan as of February 28, 2020. The deferral will be of principal, without the bank having any discretion. A bank can also permit a deferral of interest in addition to the deferral of the principal.	- Customers who have already deferred their payments for a period of up to 6 months **can obtain an additional deferral up to December 31, 2020,** on condition that the loan was not in arrears as of February 28, 2020. - Customers who have not deferred payments and are now interested in doing so can obtain a **deferral of up to 6 months**. This will also apply to customers whose loans were in arrears during two months prior to the date for submitting a request.		Addition of payments at the end of the loan period. ***		

Business credit	A business with annual turnover of NIS 25 million that was adversely affected by the crisis. The loans were serviced on schedule during the year up to February 18, 2020 and it is expected that the business will weather the crisis and will be able to service the loan after the crisis.	Up to 6 months, **at the bank's discretion.**		Addition of payments at the end of the loan period.***		

Comments:
* Not including a borrower in the midst of legal proceedings.
** Not including loans in commercial cooperation with a third party.
*** The method of rescheduling the loan payments is subject to the technical restrictions derived from the bank's computer system. If necessary, alternative solutions will be proposed for the rescheduling mechanism.
**** The interest rate – The deferred payments will bear an interest rate that does not exceed the rate in the loan agreement. It is important to emphasize that the deferral of the loan is equivalent to taking out a new loan equal to the deferred amount.

Deferrals made between March and September 2020 in Israel's banking system

Data on the deferral of bank credit repayments, March 1, 2020 to October 23, 2020					
	Consumer	**Housing**	**Small business**	**Business Commercial**	**Total**
Number of loans on which payments were deferred	458,853	180,925	172,743	8373	820,894

Total deferral (in millions of shekels)	1,904	3,072	3,448	1,950	10,376
Proportion of credit portfolio	11.6 percent	25.3 percent*	21.5 percent	6.7 percent	16.2 percent

***** Housing credit for which payment is deferred as of August 2020 accounts for about 12 percent of the housing credit portfolio.

The loan repayment deferral program for credit card companies

	Customer Group	Deferral Period	Last Date for Requesting a Deferral	Method of Rescheduling the Payments	Maximum Interest Rate	Charging of Fees
Consumer credit up to NIS 100,000 *	Customers who are paying their loans on schedule. The deferral will be only of the principal, without the company having any discretion. The company can also allow for a deferral of the interest in addition to the principal.	3 months. In addition, there is an option to extend for another 3 months (up to 6 months total), at the company's discretion.	December 31, 2020	Addition of payments at the end of the loan period.**	The interest rate specified in the original loan agreement.	The deferral will be carried out without any fee.

Business credit	A business with an annual turnover of up to NIS 25 million that was adversely affected by the crisis. The loan was serviced on schedule and it is expected that the business will weather the crisis and will be able to service the loan after the crisis.	Up to 3 months, at the bank's discretion.				

Comments:
* Not including a borrower in the midst of legal proceedings.
** The method of rescheduling the loan payments is subject to the technical restrictions derived from by the bank's computer system. If necessary, alternative solutions will be proposed for the rescheduling mechanism.

<u>Fees Supervision Order</u>

In order to provide relief to customers in dealing with the COVID-19 crisis, and in order to help them avoid visiting the branches during the crisis and instead to carry out banking activities remotely, the Banking Supervision Department published a supervisory directive that lowers the fees for an immediate debit card, a warning letter from an attorney, and a transaction carried out by telephone. The directive will be in effect for a period of 6 months from the date of its publication in the form of a final directive.

Immediate debit card fee – full exemption from fees

An immediate debit card is a basic means of payment in which the customer's bank account is debited immediately. The card makes it possible for pension recipients to withdraw money from an ATM without having to stand in line for a teller, and thus reduces the number of visits to the bank branches. As of now, there is a monthly fee of NIS 8.5 for holders of a debit card. In order to encourage wider distribution and greater use of these cards, particularly during the COVID-19 crisis, the Banking Supervision Department decided to provide an exemption from the fee for using the card during the period of the directive.

A teller-executed transaction carried out by phone – maximum fee will be NIS 2.5 per transaction

A transaction in a current account carried out by phone with a live teller is considered to be a teller-executed transaction, and accordingly the fee for a teller-executed transaction is charged, i.e. NIS 6 on average, compared to about NIS 1.5 charged for a customer-executed transaction. In order to encourage customers to avoid visiting the branches during the COVID-19 crisis and instead to carry out transactions by phone, the Banking Supervision Department decided that the maximum sum that a customer can be charged for a phone-based transaction during the period of the directive will be NIS 2.5.

A warning letter from an attorney – maximum fee will be NIS 50 per letter

When a customer does not pay a debt on schedule and all of the bank's collection attempts have been exhausted, the bank sends the customer a warning letter from an attorney to alert him about the debt before the bank sends it to the legal system for collection. The goal is to provide an opportunity for the customer to deal with the debt and thereby avoid the initiation of expensive legal proceedings and further deterioration in his situation. The fee for sending the letter ranges from NIS 147 to NIS 200. In order to provide relief to customers whose situations have deteriorated, the Banking Supervision Department decided to reduce the fee for the letter to a maximum amount of NIS 50 during the period of the directive.

Letter from the Supervisor of Banks to the banking system concerning customers who are in financial distress due to the COVID-19 crisis

In view of the high rate of unemployment and the decline in business activity, many households and businesses continue to be affected by the COVID-19 crisis. In view of this, the Supervisor of Banks distributed a letter within the banking system in which he made clear how the banks should operate, with the goal of assisting customers in financial distress due to the crisis.

The Supervisor's letter emphasized that according to the existing Banking Supervision Department directives, in the event that a customer is in financial distress and is having difficulty meeting his obligations to the bank, the bank must try as much as possible to exhaust various ways of collecting the debt, including all of its components, before turning to the legal system, while maintaining fairness and transparency during the course of the debt collection process.

This is even more relevant during the COVID-19 crisis, and the banks should therefore make even greater efforts than in normal times in order to continue operating in this manner. The goal is to identify distress and to help customers resolve this challenging situation as quickly as possible, in order to help prevent the inflation of their debts and further deterioration in their situation.

Reduction of the banking system's required leverage ratio in order to support economic activity

In view of the continuing COVID-19 crisis and the accompanying cash flow difficulties being experienced by households and businesses, there is a need to ensure that the requirement that the banking system meet a minimum leverage ratio[16], which was determined during normal times, will not constitute a barrier to providing credit during the crisis period. As a result, it was decided, by means of a temporary directive, to reduce the minimum rate to 5.5 percent for the large banks (as opposed to 6 percent today) and to 4.5 percent for the midsize and small banks (as opposed to 5 percent today).

[16] Calculated as the ratio of Common Equity Tier 1 Capital to total exposures, according to the Basel III rules.

Box 2: An examination of the banking system's resilience on the basis of statistical tools for the analysis of stress tests, based on the Research Department's macroeconomic forecast scenarios as of May, 2020

- In view of the COVID-19 crisis and its effect on economic activity in general and the banking system in particular, the Banking Supervision Department carried out an analysis of macroeconomic stress tests in May 2020 based on two scenarios for the development of the crisis. The two scenarios were based on macroeconomic forecasts made by the Bank of Israel Research Department in May of 2020.
- The goals of the analysis were the early identification of foci of risk in the banking system resulting from the crisis, and an assessment of the banking system's ability to continue its support of economic activity through the provision of credit. In addition, the analysis provided a tool to assist in decision making with regard to the policy measures required from the banking system's point of view in order to support and rehabilitate the economy.
- Unlike previous scenarios, it was assumed that growth in total credit would not be less than 2.5 percent, with the goal of assessing the banking system's ability to continue supporting the economy during the crisis.
- The results of the test indicated that even in a scenario of only a low level of control of the pandemic, including a renewed outbreak of infection in the fourth quarter of 2020 and another round of economic shutdowns, the banking system is expected to maintain its resilience and stability. The banks' capital adequacy ratio is not expected to fall below the required minimum in the stress scenario, despite the major losses that the banking system is expected to suffer due in part to the rise in credit losses.
- The main losses that are expected in the low control scenario occur in the credit portfolio, in view of the crisis's adverse effect on businesses and the high rate of unemployment due to the second shutdown of the economy. The consumer credit portfolio in particular is expected to show the largest losses in this scenario.
- The Banking Supervision Department will continue to monitor economic developments as a result of the response to the COVID-19 virus in particular and additional risks in general, and will work to maintain the stability of the banking system as part of its support for the economy.

a. Introduction

In normal times, the Banking Supervision Department carries out an annual macroeconomic stress test for the banking system (every year since 2012), based on a uniform scenario. The goal of the process is to better understand the risk foci to which the banking system and each of the banks are exposed. In this way the analysis assists in evaluating the strength and resilience of the system and ensuring the existence of a sufficient level of capital relative to the risk that originates from those sources. In addition, the test makes it possible to evaluate the banks' risk management processes, identify areas of vulnerability, and assess the banks' ability to estimate the risks that threaten them in a stress situation. In this context, the banks also evaluate the effects of a scenario built by the

Bank of Israel Research Department using a variety of accepted models and methods[17], while the Banking Supervision Department examines the expected effect of the scenario on each of the banks individually and on the banking system as a whole using a uniform method. The performance of these stress tests over the years has contributed to the strengthening of capital in the banking system and its adaptation to the risk profile of the banks and the domestic economy, as well as helping to improve the management of risk in the banking system.

In May of this year, in view of the developing COVID-19 pandemic and its impact on economic activity in general and on the financial system in particular, the Banking Supervision Department decided to examine the impact of two scenarios for the development of the crisis, as presented by the Research Department in the macroeconomic forecast published that month: a basic scenario and a scenario with a low level of control over infection. The analysis was carried out with the tools that the Banking Supervision Department uses in order to perform macroeconomic stress tests for the banking system. The test had several goals, including the early identification of risk foci in the banking system in view of the crisis, and an assessment of the banking system's ability to continue supporting the economy through the provision of credit. In addition, it constituted a tool that can assist in the determination of the necessary steps to be taken with regard to the banking system in order to support and rehabilitate the economy.

The results indicate that the realization of the more pessimistic scenario, including a renewed outbreak of the virus in the last quarter of 2020 and another shutdown of the economy, will have a significant effect on the banking system. **However, the banking system is expected to maintain its resilience and stability, and the capital adequacy ratio is not expected to decline for any of the banks to below the minimum level required by the Banking Supervision Department in the stress test, i.e. a Common Equity Tier 1 Capital ratio of 6.5 percent**, despite the large losses expected for the banking system partly due to the increase in credit losses.

As mentioned, and according to the forecasts published in May, the test was based on two scenarios: the basic scenario and a scenario of low control over infection (Figure 1), where the second scenario includes a renewal of the pandemic during the final quarter of 2020, which leads to a second shutdown of the economy, although its economic effect is less severe. The scenario includes an additional contraction in GDP, alongside an increase in unemployment, a drop in housing prices, and a shock to the capital market. It is important to emphasize that the scenario is based on assessments and models, and does not constitute a forecast.

The starting point of the scenario is December 2019 and its horizon is three years, i.e. until the end of 2022. The analysis uses actual data reported by the banking system for March 2020.

b. Assumptions

The Banking Supervision Department performed the examination based on various assumptions, with the goal of assessing the scenario's impact on each of the banks and better understanding the risk foci to which each bank is exposed. Unlike previous scenarios, **underlying this scenario is**

[17] The banks evaluated in the stress test are Leumi, Hapoalim, Discount, Mizrahi-Tefahot, First International, Union Bank, and Bank of Jerusalem.

the assumption of at least 2.5 percent growth in total credit, with the goal of determining the banking system's ability to continue supporting economic activity during the crisis. Given this level of growth in credit, an increase in assets was assumed that would facilitate it, and particularly that the entire increase in credit would be financed by attracting additional deposits from the public. In addition, as in previous years, it was assumed that there is no change in the size or the mix of the portfolio of securities, that there is no raising of additional capital, and actions taken by the banks' managements in response to the crisis with the goal of minimizing damage are not taken into account.

The results reflect the scenario's direct effect on capital, profitability, the credit portfolio, and the securities portfolio. This examination does not consider the possibility of a drop in the banks' liquidity or feedback effects such as those resulting from a loss of confidence among investors.

c. Findings

A renewed shutdown of the economy, and in particular the accompanying macroeconomic shocks, is expected to have a significant effect on the banking system, but not to endanger its stability. The shutdown of the economy, which is reflected in various restrictions placed on the labor market, leads to an increase in unemployment and a decline in business activity according to the scenario. This shock is liable to make it difficult for some sections of the public to meet their obligations, and is therefore expected to result in significant losses to the banks' credit portfolio. The shocks are also reflected in a rise in bond yields and a drop in share prices, which reduce the income from the banks' securities portfolio. Alongside the effect on the banks' profits and the erosion of banking capital during the scenario, the growth in credit in the economy increases the banking system's risk assets, and therefore acts to further erode the capital ratios. Nonetheless, the growth in credit also has a moderating effect on the damage to the banks, since it leads to an increase in interest income in the system.

It was found that despite the adverse effects, the banks maintain a Common Equity Tier 1 Capital ratio above the threshold required by the Banking Supervision Department in a stress test (6.5 percent). This result emphasizes the **importance of the capital strengthening process** (an increase of about 3 percentage points in the Common Equity Tier 1 Capital ratio during the past decade) **carried out by the Banking Supervision Department in recent years**. This is in addition to steps taken by the Banking Supervision Department to achieve more conservative risk management among the banks, including a significant reduction in the banks' exposure to large borrower groups, a reduction in exposure to credit for the purpose of acquiring control and leveraged credit, an improvement in the characteristics of the housing credit portfolio, and an improvement in the banking system's performance as a result of steps taken to improve efficiency and cut costs. The average Common Equity Tier 1 Capital ratio in the system is liable to drop in the pessimistic scenario from a level of about 11.1 percent in 2019 to about 10.2 percent in 2022 (Figure 2).[18] Although the capital ratio of the system as a whole is not significantly affected during the scenario, there is a high level of variance among the banks with respect to the scope of the decline. The bank that suffered the greatest effect fell to a capital ratio of 7.8 percent (Figure 2).

[18] The year in which the average capital ratio in the system reaches its lowest point during the scenario.

It appears that during the period of the analysis, the banks' profitability is expected to be adversely affected, **with all of the banks experiencing at least one quarterly loss during the scenario, and on average the banking system is expected to show losses for an entire year.** The average return on equity (ROE) in the system is expected to drop from 8.3 percent at the start of the scenario to -2.75 percent at the peak of the crisis (the first quarter of 2021; Figure 3).

The main losses expected in the scenario occur in the credit portfolio. The adverse effect on businesses and the high unemployment make it difficult for households and the business sector to meet their commitments, which leads to significant losses in the banks' credit portfolios and a reduction in their equity capital.

Consumer credit shows the highest rate of losses in the scenario (an average annual loss rate of about 2.1 percent)[19], which is primarily due to the sharp increase in the unemployment rate. The high loss rates are also reflected in high loss rates relative to capital (2.4 percent), even though the banking system has reduced its exposure to this portfolio during the past two years. With respect to business credit (excluding construction and real estate), the models foresee an average loss rate of 1.2 percent. The l banking system's significant exposure to this type of credit results leads to a higher rate of loss relative to capital, which stands at 1.9 percent (Figure 4).

The drop in housing prices in the scenario is also expected to result in credit losses, via the portfolio of credit to the construction and real estate industry. With respect to the credit losses in the housing credit portfolio, the rising unemployment is expected to increase the proportion of borrowers that will have difficulty making their mortgage payments, thus increasing the rate of loss in the portfolio. Nonetheless, the many steps taken by the Bank of Israel in recent years has significantly reduced the loss rates expected from this portfolio.

Another source of expected losses is the securities portfolio, in view of a sharp rise in bond yields and declines in share prices. Currently, the banks manage a conservative securities portfolio, which is made up primarily of low-risk securities, namely Israeli government bonds (about 57.6 percent of the portfolio in December 2019). Nonetheless, the rise in the yields on government bonds, as a result of the nature of the scenario, leads to a drop in their value and therefore to significant losses.

The pessimistic scenario is characterized by a high level of severity, which is similar to that used in past stress tests, and which reflects risk foci to which the Israeli economy and the banking system are exposed during the COVID-19 crisis. It should again be emphasized that the scenario was constructed on the basis of developments in the economy up until the month of May. The Bank of Israel Research Department continues to update the macroeconomic forecasts according to recent economic developments, including the high rate of unemployment and the introduction of additional restrictions on economic activity. In this context, a deterioration is expected in the various scenarios for the development of the crisis. The Banking Supervision Department will continue to monitor the risks faced by the banking system, in accordance with the updated forecasts.

[19] Based on models and assessments, and not meant to be a forecast.

Figure 2.1
Historical Macroeconomic Data and Development of Scenarios, 2000–2022

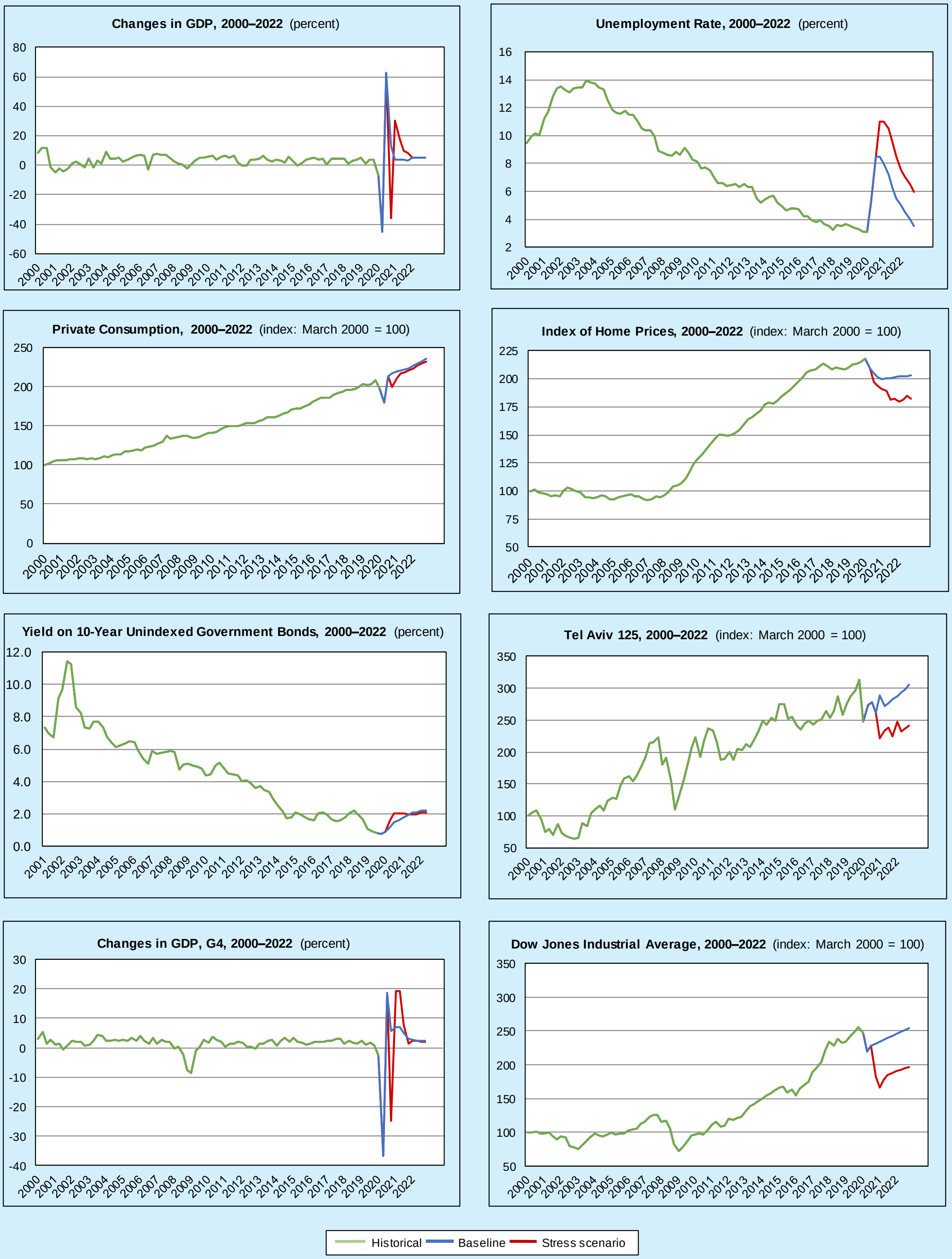
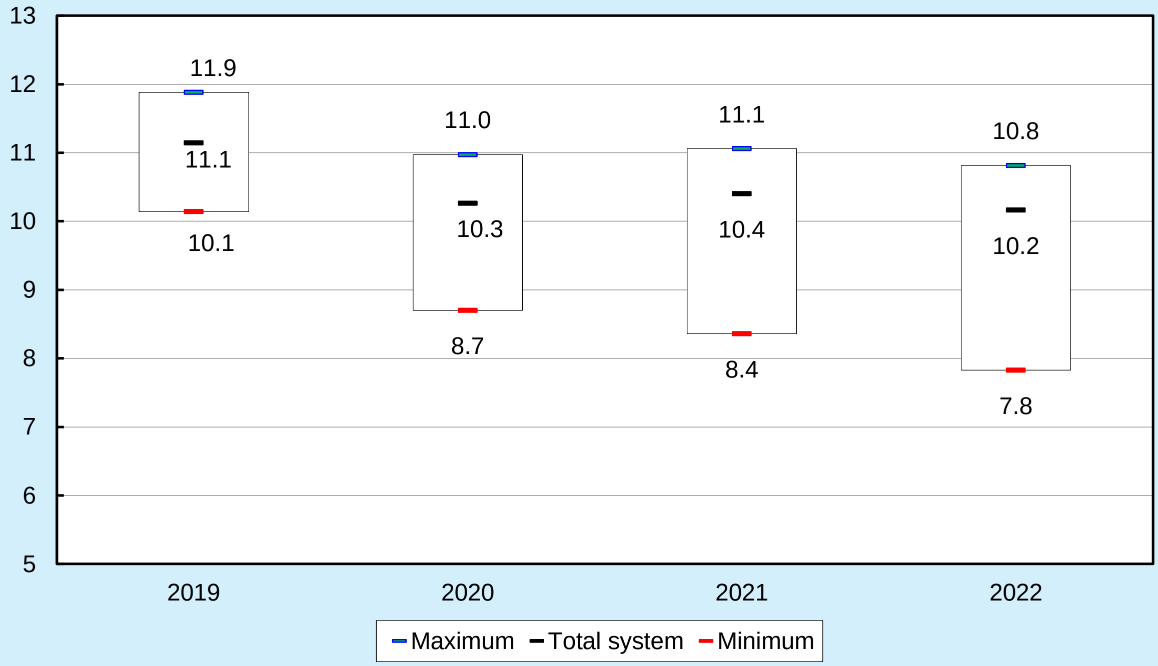
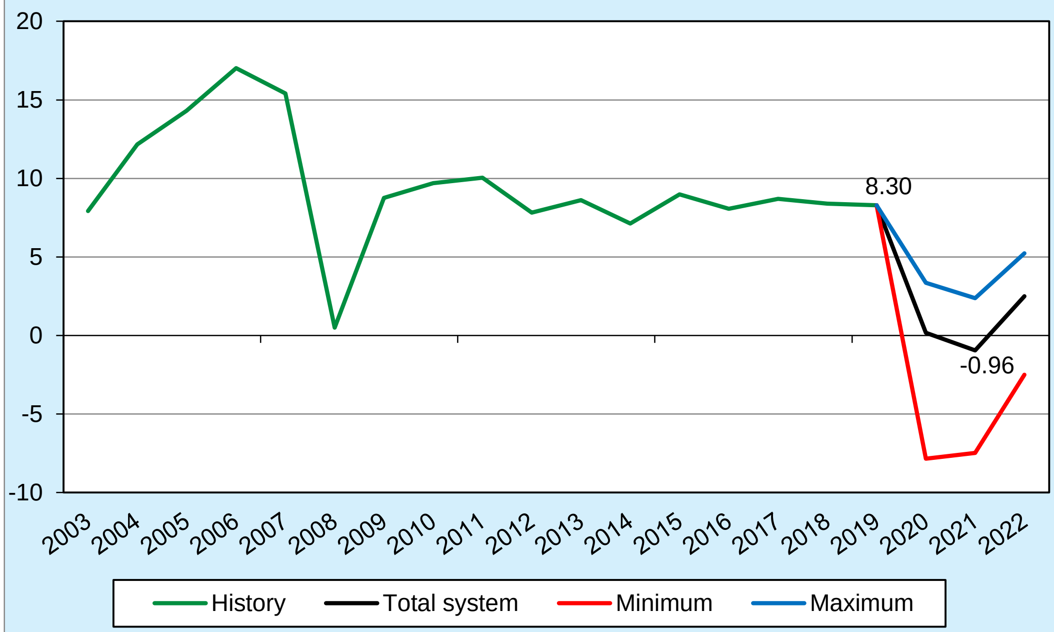


Figure 2.2
Development of Tier 1 Capital Ratio According to the Banking Supervision Department's Stress Test, Total System, 2019–2022[a]



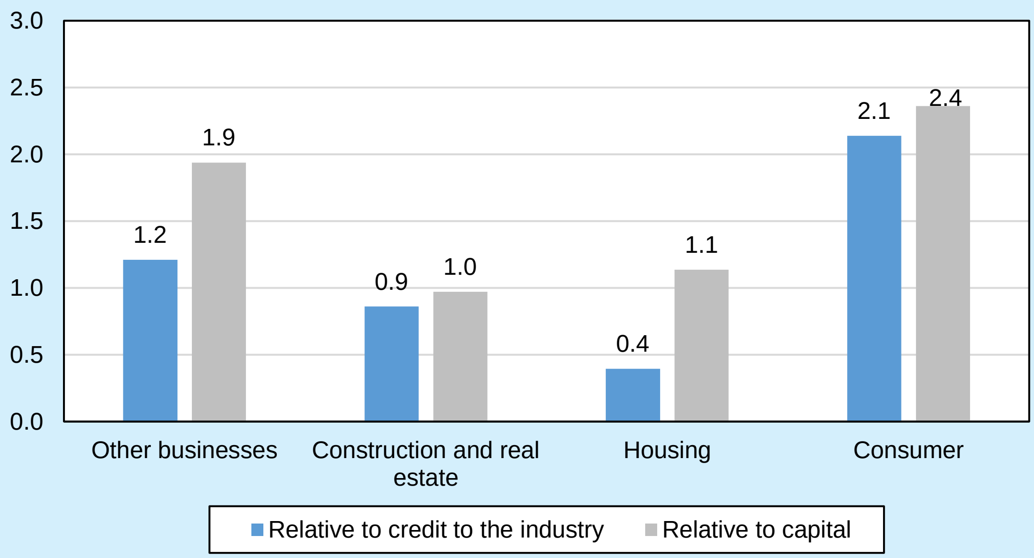
[a] Based on models and assessments, and not as a forecast.
SOURCE: Banking Supervision Department.

Figure 2.3
Development of Return on Equity According to the Banking Supervision Department's Stress Test, Total System, 2003–2022[a]



[a] Based on models and assessments, and not as a forecast.
SOURCE: Banking Supervision Department.

Figure 2.4
Expected Loan Loss Provisions During the Stress Test[a,b], Selected Industries, Total System, 2020–2022 Average



[a] Based on models and assessments, and not as a forecast.
[b] Total credit losses relative to capital are 7.1 percent, credit losses relative to capital are across all segments.
SOURCE: Banking Supervision Department.