



BANK OF ISRAEL

FINANCIAL STATEMENTS FOR 2021

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Bank of Israel

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CONTENTS

	Page
Financial Highlights	5
Auditors' Report	15
Statement of Financial Position	16
Statement of Profit or Loss and Other Comprehensive Income	18
Statement of Allocation of Profits (Losses)	19
Statement of Changes in Deficit Equity	20
Statement of Cash Flows	21
Notes to the Financial Statements	23

FINANCIAL HIGHLIGHTS FOR 2021

The Covid-19 Crisis and its Effect on the Financial Statements

In response to the global economic crisis resulting from the worldwide outbreak of the Covid-19 pandemic in early 2020 and congruently with other central banks around the world, the Bank of Israel exercised a series of tools designed to cope with the ongoing crisis to secure the regular operation of the domestic financial markets, facilitate credit terms in the market, and support its economic activity and financial stability.

The steps adopted in response to the crisis include buying government bonds in local currency; buying corporate bonds in local currency; providing the banking system long-term loans for extending credit to small businesses; entering into reverse repos as bond collateral; and entering into dollar/shekel swaps.

To achieve its monetary policy objectives and supporting the economy's recovery from the crisis, the Bank of Israel continued to use some of these tools in 2021 such as buying government bonds; providing long-term monetary loans; and entering into reverse repos.

The Bank of Israel also continued to purchase foreign exchange as a monetary tool used at the time of the crisis to sustain the Bank's objectives and the economic recovery from the Covid-19 crisis. In 2021, the Bank purchased a total of about \$34.8 billion.

In 2020–21, as a result of the use of the special market tools discussed above, the Bank's balance sheet increased by about NIS 369.1 billion, to about NIS 809.4 billion at the end of 2021, an increase of some 83.8 percent. The activity also affected the Bank's financial results, as reflected in the rise in the Bank's revenue from foreign exchange reserves and the local tools used, but also enhanced the Bank's exposure to exchange rate fluctuations due to the increase in its foreign exchange reserves. In 2020–21, the Bank incurred significant expenses in respect of exchange rate differentials due to the appreciation of the shekel against the other investment currencies.

In this context it should be noted that the Bank of Israel fulfills its duties as a central bank and acts to achieve its objectives as set forth in the Bank of Israel Law, 5770-2010 ("the Bank of Israel Law"); The Bank's activity for meeting its objectives and performing its functions is not aimed to maximize any profits but rather to maximize nationwide economic benefits.



Initial Adoption of IFRS

The financial statements have been prepared in conformity with International Financial Reporting Standards ("IFRS").

The Bank first applied IFRS in these financial statements as a step toward conforming to the accepted and updated international reporting framework which better reflects the prevailing business and economic conditions and enhances the readers' trust and the transparency of the Bank's financial reporting.

Before 2020, the Bank prepared financial statements in conformity with generally accepted accounting principles in Israel ("Israeli GAAP"), as adjusted to the special functions of a central bank¹. The main item presented in accordance with generally accepted accounting principles applicable to other central banks is revaluation accounts.

As per the Bank of Israel Law, unrealized gains² are not included in the Bank's net income³. Through the financial statements for 2020, these gains were not included in the Bank's net income but rather were carried to the revaluation accounts under the Bank's liabilities.

On the date of transition to IFRS reporting, unrealized gains from exchange rate differentials and from fair value revaluation of financial assets are included in the Bank's annual income. These amounts are then carried to the revaluation reserves in equity until they are realized. According to IFRS, changes in the actuarial calculation of employee benefit liabilities are carried to a capital reserve in Other Comprehensive Income.

The reconciliations of the annual income (loss) as per IFRS to the net income (loss) defined in the Bank of Israel Law, which is used to determine the profits that are distributable to the Government, are disclosed in the statement of Allocation of Profits (see Note 23 to the financial statements).

The Bank's Statement of Financial Position (Balance Sheet)

At the end of 2021, the Bank's Balance Sheet totaled approximately NIS 809.4 billion, an increase of about NIS 163.4 billion (about 25.3 percent) compared with the end of 2020. The increase in the Bank's Balance Sheet was mainly affected by foreign currency purchases and the increase in other assets in keeping with the steps taken by the Bank of Israel for contending with the Covid-19 crisis.

The increase on the asset side mainly results from the following:

- (1) An increase of approximately NIS 108.1 billion in "Total assets abroad", mainly owing to foreign currency purchases by the Bank in the context of

¹ As per Section 75 of the Bank of Israel Law, the financial statements are to be prepared "... in accordance with generally accepted accounting principles as adjusted to the special activity of a central bank".

² Gains on assets which the Bank keeps holding as part of its asset portfolio.

³ Section 76 of the Bank of Israel Law states that "the Bank's net income in the previous year, as presented in the annual financial statements, shall not include profits not yet realized as set forth the annual financial statements".



implementing its monetary policy and assisting the local economy following the crisis.

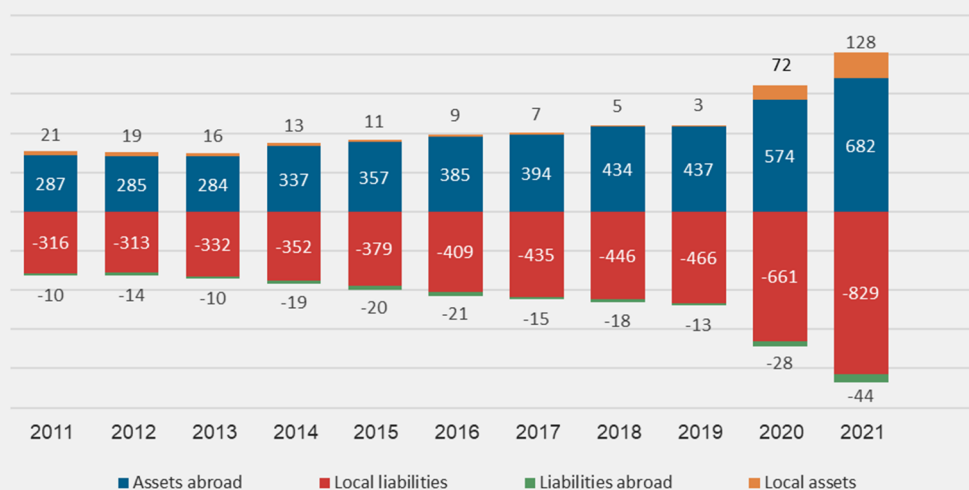
- (2) An increase of approximately NIS 55.3 billion in "Local assets", arising from the measures adopted by the Bank in response to the financial implications of the Covid-19 crisis consisting mainly of pursuing the plan to buy local currency government bonds at a scope of about NIS 38.5 billion and granting long-term loans to the banking system for extending credit to small businesses at a scope of about NIS 20.4 billion.

The increase in the Bank's assets as discussed above is mirrored by a corresponding increase on the liability side, with about NIS 137 billion carried to monetary absorption instruments— Short-term bills (*Makam*) and time deposits—arising from the need to absorb excess cash created in the markets from these purchases.

The composition of assets and liabilities in the Bank's financial statements is indicative of a major currency imbalance. The majority of the Bank's assets are denominated in foreign currency whereas the cast majority of the Bank's liabilities are denominated in NIS.

The increase in the Bank's Balance Sheet (Figure 1), which was mainly affected by the increase in foreign exchange reserves, aggravated the currency imbalance inherent to the Bank's Balance Sheet and the dependence of the Bank's profits on gains from exchange rate differentials and the degree of their volatility.

Figure 1
The Developments in the Bank's Assets and Liabilities, 2011-2021
(NISbillion)



Source: Bank of Israel



Foreign Exchange Reserves

In 2021, foreign exchange reserves grew by about NIS 105.2 billion to about NIS 662.4 billion, which is equivalent to about \$213 billion (Table 1).

The increase in foreign exchange reserves is mainly a result of dollar purchases in an aggregate of some NIS 112.1 billion (about \$34.8 billion) made by the Bank in the context of its monetary policy to support the achievement of the Bank's objectives and to help the Israeli economy to recover from the Covid-19 crisis.

The allocation of SDRs of the IMF enhanced the reserves by about NIS 8.4 billion (about \$2.6 billion) as part of the IMF's allocations in an aggregate of some \$650 billion to all member states in an attempt to increase global reserves, promote the stability of the global economy and assist underprivileged states in dealing with the economic consequences of the pandemic.

The private sector and the Government combined contributed about NIS 5 billion to the foreign exchange reserves.

Table 1
Contribution of sectors to the change in the foreign exchange reserves

	2021	2020	2021	2020
	NIS million		USD million	
Change in foreign exchange reserves	105,242	121,644	39,701	47,283
Bank of Israel				
Purchases	112,143	72,136	34,797	21,238
Profits	15,956	20,701	5,348	6,626
Exchange rate differentials	(36,307)	(25,186)	(4,672)	(3,743)
Other ¹	8,456	78	2,628	8,197
Total Bank of Israel	100,248	67,729	38,101	32,318
The Government²	(1,404)	52,195	(462)	14,634
The private sector³	6,398	1,720	2,062	331

¹ Includes the allocation of SDRs by the IMF in an aggregate of NIS 8.4 billion (about \$2.6 billion) and the Bank's payments and receipts in foreign currency.

² Transfers from abroad by the Government and national institutions.

³ Includes payment of the segment's income tax in foreign currency.



Gains from Foreign Exchange Reserves and Exchange Rate Differentials

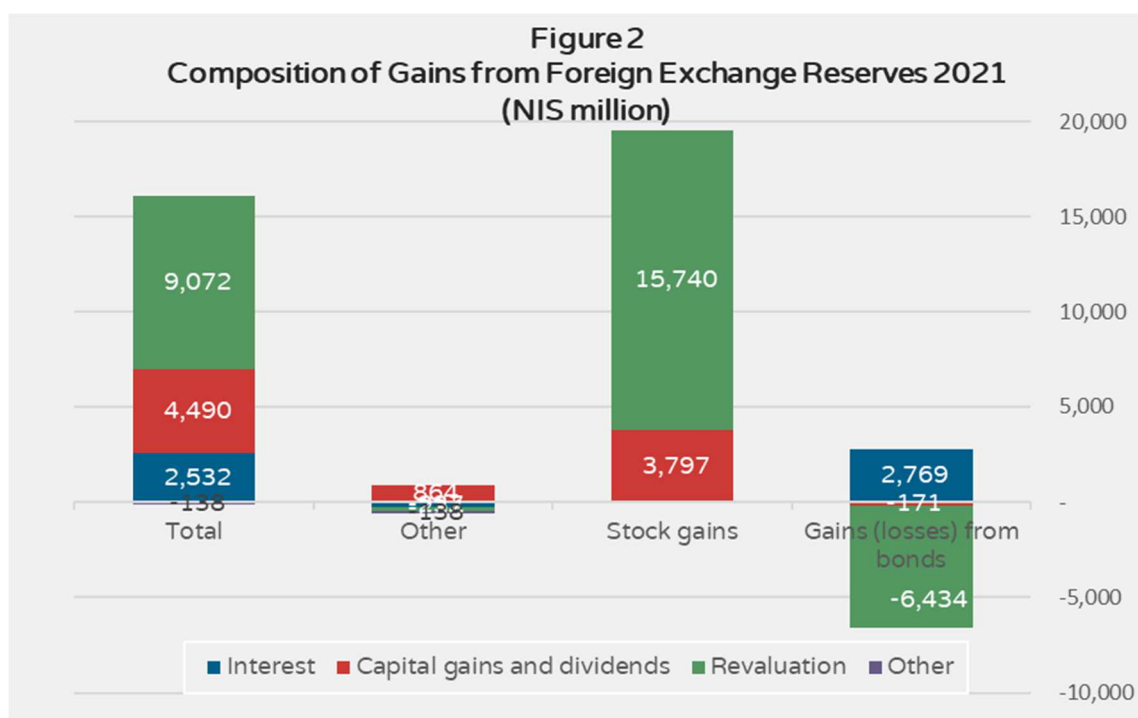
In 2021, gains from foreign exchange reserves, excluding exchange rate differentials, amounted to about NIS 16 billion (2020 - about NIS 20.7 billion).

The gains mostly derived from stock market increases in the year, mainly in the U.S. stock market which experienced the highest markups among the stock markets in which the Bank of Israel invests, and in which it invests in higher rates compared with other markets. The increases were a result of major improvements in corporate business profits recorded in 2021 as opposed to 2020 and the absence of investment alternatives due to low real returns⁴.

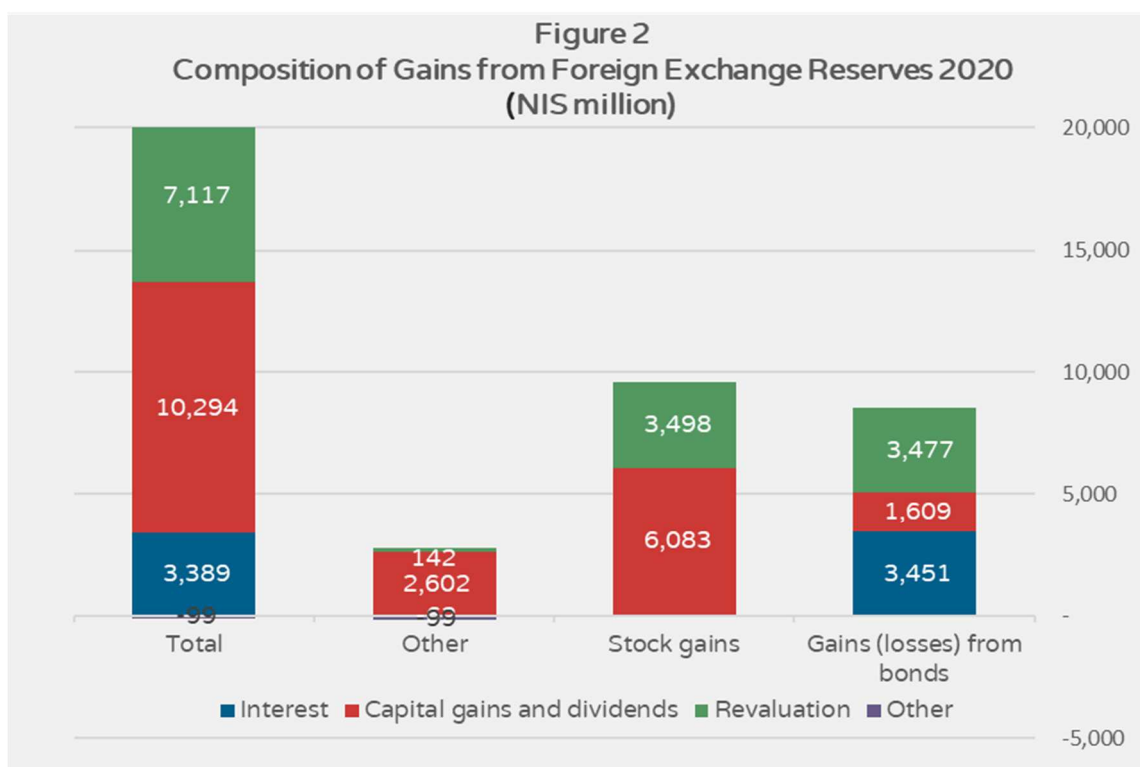
The increase in foreign exchange reserves was accompanied by a corresponding increase in the Bank's relative investments in risk assets. The return on risk assets is expected to be higher on average than the return on other less risky assets and enhances the expected return on the reserves. At the end of 2021, equity investments accounted for 18 percent of the reserve portfolio.

In contrast, in the year, the Bank recorded losses from bond revaluation due to the rise in yields towards year end.

The following figures present the composition of gains from foreign exchange reserves in 2020 and 2021:



⁴ See the Bank's report of foreign exchange reserve investments for 2021 issued separately from these financial statements.



In 2020, a substantial portion of the gains derived from stock portfolio realizations and to a lesser extent from bond realizations whereby both investment channels ended the year with revaluation gains.

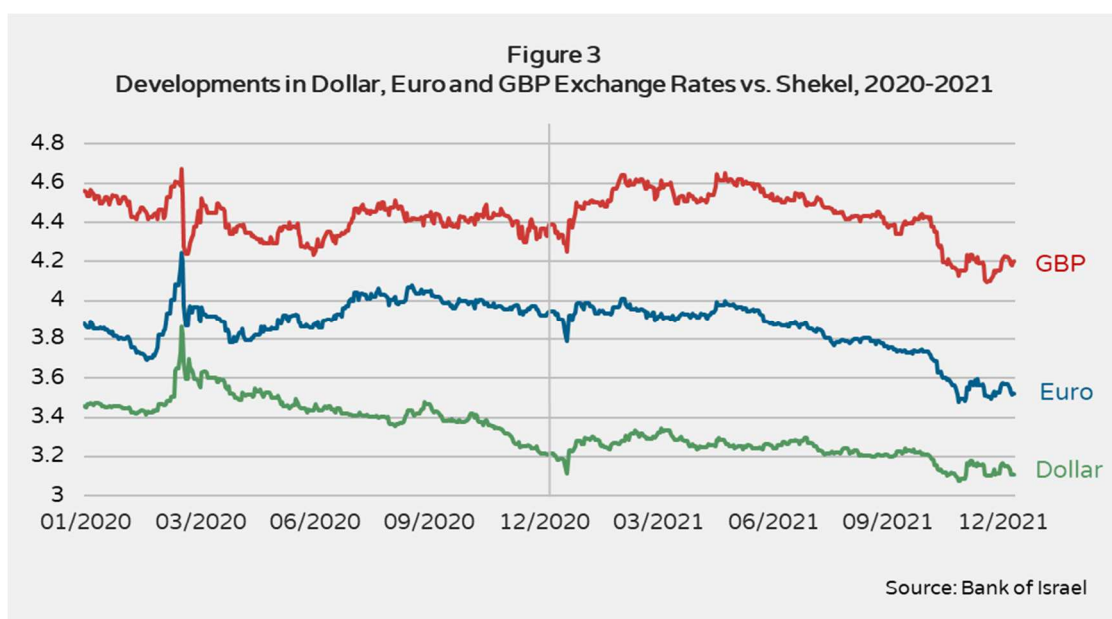
Exchange Rate Differentials on Foreign Exchange Reserves

The Bank's financial statements are presented in local currency and therefore, changes in the shekel exchange rate in relation to the currencies in which the foreign exchange reserves are denominated are likely to cause large fluctuations in the NIS value of the reserves. The Bank does not use any instruments to hedge the effect of these changes and accordingly the fluctuations are reflected in the Bank's profits.

Notwithstanding the aforesaid, due to the consistent increase in the Bank's foreign exchange reserves, substantially all gains from exchange rate differentials are not realized whereby changing trends in the shekel against the currencies underlying the reserve portfolio are likely to offset their effect.

In 2021, the Bank recorded losses of about NIS 36.3 billion from exchange rate differentials on foreign exchange reserves arising from the major appreciation of the shekel mainly against the euro and to some degree against the dollar. Offsetting these losses against NIS gains on foreign exchange reserves led to a negative return of about 2.9 percent in NIS terms.

(In 2020, losses from exchange rate differentials of about NIS 25.2 billion were recorded as a result of the shekel's appreciation, mainly against the dollar) (Figure 3).



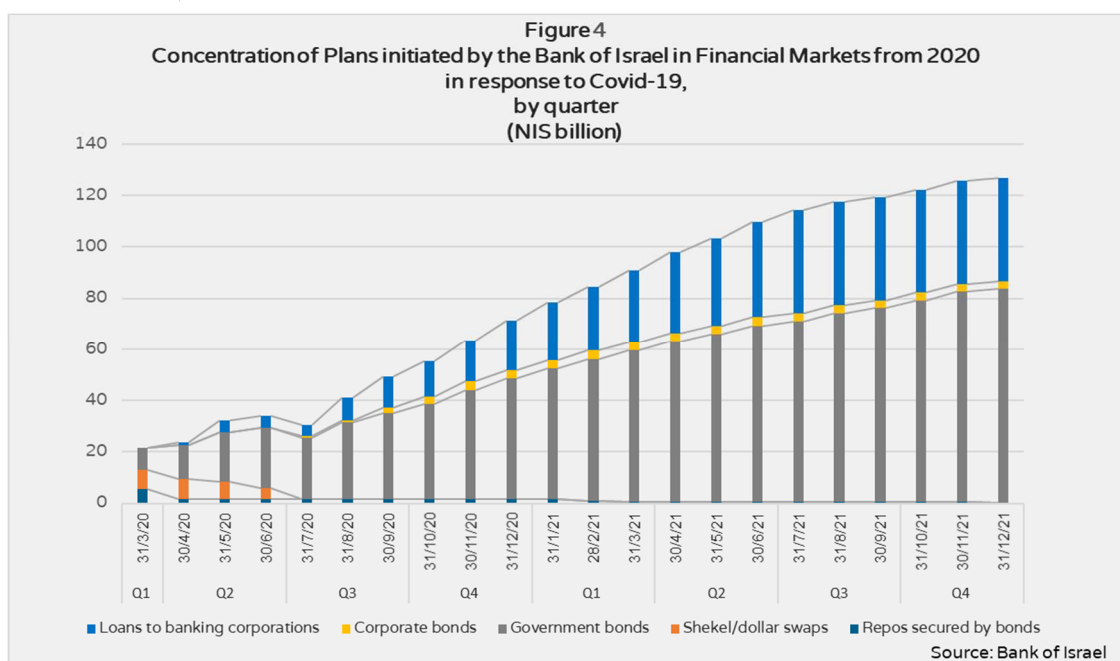
Local Assets

Against the backdrop of the global macroeconomic crisis arising from the outbreak of the Covid-19 pandemic in 2020, the Bank of Israel initiated several plans to address the financial system's cash distress caused by the crisis to ensure the operating continuity of the financial markets, facilitate market credit terms and support the economic activity and financial stability.

In 2021, the Bank continued to use some of the tools at its disposal to achieve the objectives of the monetary policy to support and sustain the local market's recovery such as buying government bonds; providing long-term monetary loans; and entering into reverse repos.

In 2021, an increase of about NIS 55.3 billion was recorded in local assets (Figure 4), deriving mainly from the following:

- (1) An increase of about NIS 36.6 billion in local government bonds as part of the purchase plan implemented in 2021 with related interest income amounting to NIS 0.9 billion.
- (2) An increase of about NIS 20.4 billion in loans granted to banking corporations for enlarging the credit facilities extended by the banks to small and very small businesses in the wake of the Covid-19 crisis with related interest income amounting to NIS 21.6 million.



Local Liabilities

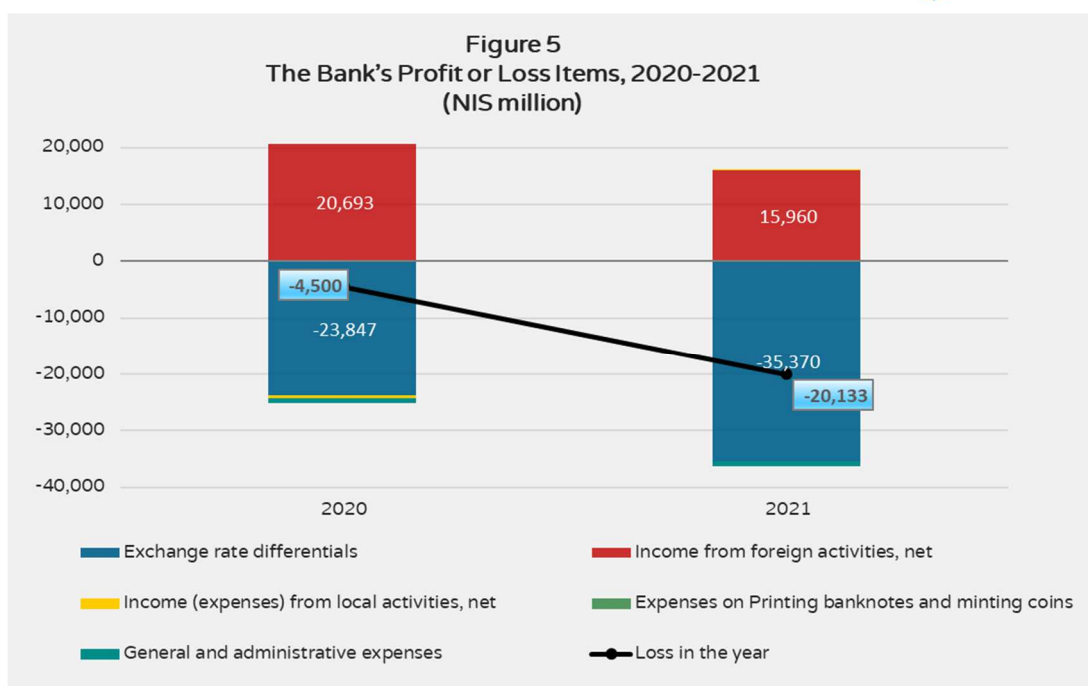
The majority of local liabilities consist of Short-term bills (*Makam*) and time deposits, monetary tools which are used to absorb excess cash in the market.

In 2021, *makam* and time deposits grew by about NIS 137 billion to NIS 589 billion. The Bank's foreign currency purchases in 2021 and the increase in local monetary tools exercised by the Bank in response to the crisis led to cash inflows in the market which were absorbed by the Bank. Despite the increase in these balances, the expenses in their respect decreased in 2021 by about NIS 81 million to NIS 453 million, mainly due to the decline in the average yields on *makam* in the year.

Statement of Profit or Loss

In 2021, the Bank recorded a loss of about NIS 20.1 billion (2020 – a loss of about NIS 4.5 billion). Gains from foreign exchange reserves without exchange rate differentials totaled about NIS 16 billion, mostly deriving from stock appreciation gains and partly offset by bond revaluation losses due to the increase in yields. In contrast, the main cause for the loss in the year in NIS terms is exchange rate losses totaling about NIS 35.4 billion as a result of the major appreciation of the shekel against the euro and dollar.

Figure 5 presents the main items of the Bank's Statement of Profit or Loss.



The Bank's Equity and Revaluation Reserves

At the end of 2021, the Bank's deficit equity and revaluation reserves totaled about NIS 63.5 billion, as opposed to about NIS 43 billion last year.

The Bank's year end accumulated deficit net of revaluation reserve transfers was approximately NIS 103.7 billion, as opposed to about NIS 74.3 billion last year.

The amounts transferred to revaluation reserves as per IFRS consist of changes in the Bank's actuarial accrual for employee rights arising from changes in actuarial assumptions and unrealized gains from fair value revaluation of assets included in the Bank's profit or loss but excluded from the net income which is used to determine the profits distributable to the Government as per the Bank of Israel Law. When these gains are realized, they are reclassified from the revaluation account and included in distributable net profits.

According to the Bank's former reporting framework, these unrealized gains were not included in the Bank's net income but rather in the revaluation accounts as part of the Bank's liabilities. Upon the transition to IFRS reporting in 2021, these reserves are included in the Bank's annual income and equity. It should be noted that this accounting change has no effect on the calculation of the profits distributable to the Government per law.

Revaluation reserves deriving from unrealized gains increased from NIS 27.3 billion in 2020 to NIS 36.2 billion in 2021. The main increase stems from unrealized stock appreciation gains offset by the impairment of foreign currency bonds at year end due to the decline in yields.



AUDITORS' REPORT

To the Governor and the Supervisory Council of the
BANK OF ISRAEL

We have audited the accompanying Statements of Financial Position of the Bank of Israel ("the Bank") as of December 31, 2021 and 2020 and January 1, 2020, and the related Statements of Profit or Loss and Other Comprehensive Income, Changes in Deficit Equity and Cash Flows of the Bank for each of the years ended December 31, 2021 and 2020 ("the financial statements") featured on pages 16-78 below. These financial statements are the responsibility of the Bank's Supervisory Council, Governor, Director General and Director of the Accounting, Payment and Settlement Systems Department. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in Israel, including those prescribed by the Auditors' Regulations (Auditor's Mode of Performance), 1973. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the Bank's management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Bank as of December 31, 2021 and 2020 and January 1, 2020, and the results of its operations, changes in its deficit equity and cash flows for each of the years ended December 31, 2021 and 2020, in conformity with International Financial Reporting Standards ("IFRS").

Tel-Aviv, Israel
March 27, 2022

Kost Forer Gabbay and Kasierer
KOST FORER GABBAY & KASIERER
A Member of Ernst & Young Global



STATEMENT OF FINANCIAL POSITION

		December 31,		January 1,
		2021	2020	2020
	Note	NIS million		
ASSETS				
Assets abroad				
Foreign exchange reserves	3			
Cash and cash equivalents		170,870	132,735	107,928
Foreign currency securities		489,340	420,925	318,589
Derivative financial instruments		2,665	466	778
Other assets		3,779	12,383	3,798
The International Monetary Fund		14,534	6,606	6,084
BIS investment	4	398	399	384
Total assets abroad		681,586	573,514	437,561
Local assets				
Local currency bonds	5	86,654	50,345	1,677
Loans to financial institutions	5	40,128	21,061	-
Other assets	6	200	188	199
Fixed assets and Intangible assets	7	783	823	833
Total local assets		127,765	72,417	2,709
Total assets		809,351	645,931	440,270

The accompanying notes are an integral part of the financial statements.



		December 31,		January 1,
		2021	2020	2020
	Note	NIS million		
LIABILITIES				
Liabilities abroad				
Foreign exchange reserves				
Derivative financial instruments	3	345	4,042	1,078
Other liabilities	3	18,435	11,907	579
The International Monetary Fund	3c	12,013	4,100	4,236
Total liabilities abroad		30,793	20,049	5,893
Local liabilities				
Banknotes and coins in circulation	8	113,078	105,805	87,178
Reserves of banking corporations against reserve requirement	5	81,468	55,017	45,687
Time deposits	5	474,005	365,002	194,011
Short-term bills (<i>Makam</i>)	5	114,984	86,975	119,870
Government reserves	5	49,722	47,625	18,184
Other liabilities	9	8,816	8,408	7,791
Total local liabilities		842,073	668,832	472,721
Total liabilities		872,866	688,881	478,614
Bank's equity (deficit equity) and reserves				
Bank's equity (deficit equity)	10			
Bank's equity and general reserve		3,985	3,985	3,985
Accumulated deficit		(103,662)	(74,262)	(60,094)
Revaluation reserves		36,162	27,327	17,765
Total Bank's equity (deficit equity) and reserves		(63,515)	(42,950)	(38,344)
Total liabilities and equity		809,351	645,931	440,270

The accompanying notes are an integral part of the financial statements.

Prof. Amir Yaron

A. Yaron
Governor

Prof. Yehoshua (Shuki) Shemer

J. Shemer
Chairman of the Supervisory Council

Shulamit Geri

Shulamit Geri
Director General and Senior Officer in charge of Finance

March 27, 2022



STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME

	Note	Year ended December 31,	
		2021	2020
		NIS million	
Income (expenses) from activities abroad			
Gains (losses) from foreign exchange reserves			
Interest income, net	14	2,532	3,389
Gain or loss from fair value revaluation of financial assets	15	13,562	17,411
Miscellaneous expenses, net	16	(138)	(99)
Other income (expenses) from activities abroad		4	(8)
Total income from activities abroad, net		15,960	20,693
Income (expenses) from local activities			
Interest income, net	17	1,054	286
Interest expenses	17	(911)	(946)
Gain from fair value revaluation of financial assets	18	-	179
Miscellaneous income, net	19	3	15
Total income from local activities, net		146	(466)
Exchange rate differentials	20	(35,370)	(23,847)
Loss from financial activities		(19,264)	(3,620)
Expenses of printing banknotes and minting coins		38	*) 70
General and administrative expenses	21	862	*) 837
Other income, net	22	31	27
Loss in the year		(20,133)	(4,500)

*) Reclassified, see Note 21.

OTHER COMPREHENSIVE INCOME (LOSS)

Amounts that will not be subsequently reclassified to profit or loss:		
Loss from remeasurement of defined benefit plan	(431)	(121)
Gain (loss) from investments in equity instruments measured at fair value through other comprehensive income	(1)	15
Other comprehensive loss	(432)	(106)
Comprehensive loss	(20,565)	(4,606)

The accompanying notes are an integral part of the financial statements.



STATEMENT OF ALLOCATION OF PROFITS (LOSSES)*

	Note	Year ended December 31,	
		2021	2020
		NIS million	
Loss in the year		(20,133)	(4,500)
Allocation of unrealized gains to revaluation reserve	24	(11,332)	(16,323)
Recognition of gains realized in the year	24	2,065	6,655
Total loss recognized in the year		(29,400)	(14,168)

*) The statement of allocation of profits (losses) is used to calculate the net income as per Article 76 to the Bank of Israel Law (see also Note 24).

The accompanying notes are an integral part of the financial statements.



STATEMENT OF CHANGES IN DEFICIT EQUITY

	Bank's Equity		Revaluation Reserves				Total
	Bank's Equity and General Reserve	Accumulated Deficit	Other Comprehensive Income (Loss)	Unrealized Exchange Rate Differentials	Unrealized Gains from Fair Value Adjustments	Total Revaluation Reserves	
Balance as of January 1, 2020	3,985	(60,094)	(2,884)	94	20,555	17,765	(38,344)
Comprehensive income (loss)	-	(20,823)	(106)	*2,747	*13,576	16,217	(4,606)
Recognition of gains realized in the year	-	6,655	-	(410)	(6,245)	(6,655)	-
Balance as of December 31, 2020	3,985	(74,262)	(2,990)	2,431	27,886	27,327	(42,950)
Comprehensive income (loss)	-	(31,465)	(432)	*(2,098)	*13,430	10,900	(20,565)
Recognition of gains realized in the year	-	2,065	-	(268)	(1,797)	(2,065)	-
Balance as of December 31, 2021	3,985	(103,662)	(3,422)	65	39,519	36,162	(63,515)

*amounts transferred to revaluation reserves, see Note 10.

The accompanying notes are an integral part of the financial statements.



STATEMENT OF CASH FLOWS

	Year ended December 31,	
	2021	2020
	NIS million	
<u>Cash flows from operating activities:</u>		
Loss in the year	(20,133)	(4,500)
Adjustments to reconcile loss in the year to net cash provided by operating activities:		
<u>Adjustments to profit or loss items:</u>		
Interest income from foreign exchange reserves, net	(2,532)	(3,389)
Gain from fair value revaluation of financial assets, net	(13,562)	(17,411)
Other expenses (income) from activities abroad, net	(4)	8
Tax expenses on foreign investments	62	46
Interest expenses (income) on financial instruments from local activities, net	(143)	660
Gain from fair value revaluation of financial assets from local activities	-	(179)
Exchange rate differentials	35,370	23,847
Depreciation and amortization	105	103
	19,296	3,685
<u>Changes in asset and liability items:</u>		
Increase in investment in foreign currency securities abroad	(95,745)	(104,329)
Decrease in derivative financial instruments abroad	993	2,776
Decrease (increase) in collaterals on derivative financial instruments abroad	4,179	(2,743)
Decrease (increase) in short-term deposits abroad	5,340	(5,429)
Increase in reverse repos abroad	5,063	12,105
Decrease (increase) in other assets abroad	377	(435)
Increase in IMF deposits	(125)	(726)
Increase in investment in local currency bonds in Israel	(36,904)	(48,866)
Increase in loans to local financial institutions	(19,045)	(21,055)
Decrease in local derivative financial instruments	-	179
Decrease (increase) in other local assets	(6)	7
Increase in local reserves of banking corporations	26,486	10,020
Increase in local time deposits	109,000	171,000
Increase (decrease) in short-term bills (<i>makam</i>)	27,963	(33,093)
Increase in local government reserves	2,475	29,959
Increase in other local liabilities	113	614
Decrease in employee benefit liabilities	(132)	(105)
	30,032	9,879

The accompanying notes are an integral part of the financial statements.



	Year ended December 31,	
	2021	2020
	NIS million	
<u>Cash paid and received during the year:</u>		
Interest paid on reserves abroad	(254)	(102)
Interest received from reserves abroad	3,793	3,762
Interest paid on local reserves	(868)	(772)
Interest received from local reserves	1,628	479
Dividends received	2,037	1,544
Taxes on income paid	(62)	(46)
	6,274	4,865
Net cash provided by operating activities	35,469	13,929
<u>Cash flows from investing activities:</u>		
Loans granted to employees	(9)	(3)
Purchase of Fixed assets and Intangible assets	(67)	(95)
Net cash used in investing activities	(76)	(98)
<u>Cash flows from financing activities:</u>		
Increase in banknotes and coins in circulation	7,273	18,627
Net cash provided by financing activities	7,273	18,627
Exchange rate differentials on cash and cash equivalents	(4,531)	(7,651)
Increase in cash and cash equivalents	42,666	32,458
Cash and cash equivalents at beginning of year	132,735	107,928
Cash and cash equivalents at end of year	170,870	132,735
The accompanying notes are an integral part of the financial statements.		



NOTES TO THE FINANCIAL STATEMENTS

NOTE 1 | GENERAL

1. The Bank of Israel ("the Bank") is the central bank of the State of Israel. The Bank was established in 1954. It is situated in Jerusalem and has two branches in Tel Aviv. The Bank is independent in choosing its operations and in exercising its authorities in order to achieve the objectives and functions specified in the Bank of Israel Law, 5770-2010 ("the Law"). The Bank's institutions include a Monetary Committee headed by the Governor and a Supervisory Council headed by a member from among the public.

Pursuant to the Law, the Bank's functions include: managing the monetary policy; holding and managing the foreign currency reserves of the State; supporting the orderly activity of the foreign exchange market in Israel; acting as banker of the Government; regulating the economy's payment and settlement systems so as to ensure their efficiency and stability; issuing currency; regulating and guiding the cash system of the economy; and supervising and regulating the banking system. In addition, under the Credit Data Law, 5776-2016, the Bank manages the Credit Data System, gathers the credit data from the available data sources, holds the credit data in a credit pool and delivers them to the credit bureaus and to customers.

2. Following the outbreak of the COVID-19 pandemic in early 2020 and the ensuing global macroeconomic crisis, and like other central banks around the world, the Bank of Israel implemented a series of monetary tools designed to deal with the implications of the crisis to secure the normal functioning of the local financial markets, to ease credit terms and support economic activity and financial stability.

The plans implemented consist of the purchase of government bonds in local currency; the purchase of corporate bonds in local currency; the grant of long-term loans to the bank system for extending credit to small businesses; the use of reverse repo agreements with bonds as collateral; and dollar/shekel swaps.

The Bank of Israel continued to purchase foreign exchange as part of the monetary tools used during that period.

In order to achieve the monetary policy objectives and support the domestic market's recovery from the crisis, in 2021, the Bank of Israel continued to utilize some of these tools such as buying government bonds; granting long-term monetary loans; and entering into reverse repos. The Bank also announced a plan for the purchase of \$30 billion in 2021 to support achieving the Bank's targets and the market's recovery from the Covid-19 crisis. These purchases lasted through year-end after the plan had been completed. The local currency intervention plans ended in 2021.



NOTE 2 | SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies specified below have been consistently applied in the financial statements for all periods presented, unless otherwise stated.

A. Basis of reporting and measurement of the financial statements

1. The financial reporting principles

The financial statements are prepared in accordance with International Financial Reporting Standards (IFRS).

In these financial statements, the Bank first applied IFRS, including IFRS 1, "First-time Adoption of International Financial Reporting Standards".

Prior to adopting IFRS, the Bank prepared its financial statements in conformity with generally accepted accounting principles in Israel (Israeli GAAP), as adapted to the special activity of a central bank and consistent with the practice of other central banks. The Bank's last annual financial statements in conformity with Israeli GAAP were prepared as of December 31, 2020 and for the year then ended.

See Note 23 below for an explanation of the effects of the transition to IFRS on the statement of financial position and the reported financial results.

2. Measurement basis

The Bank's financial statements have been prepared on a cost basis, except for the following items:

- a. Financial assets and liabilities measured at fair value through profit or loss;
- b. The Bank's stock in the Bank for International Settlements (BIS) which are designated and measured at fair value through other comprehensive income;
- c. Employee benefit liabilities which are measured at the present value of the defined benefit plan.

B. Functional currency, presentation currency and foreign currency

The Bank's functional currency is the new Israeli shekel ("NIS").

The financial statements are presented in NIS and rounded up to the nearest million, unless otherwise stated.

1. Transactions, assets and liabilities in foreign currency

Transactions denominated in foreign currency are recorded upon initial recognition at the exchange rate at the date of the transaction. After initial recognition, monetary assets and liabilities denominated in foreign currency are translated at each reporting date into the functional currency at the exchange rate at that date. Exchange rate differences are recognized in profit or loss. Non-monetary assets and liabilities denominated in foreign currency and measured at cost are translated at the exchange rate at the date of the transaction.



2. Index-linked monetary items

Monetary assets and liabilities linked to the changes in the Israeli Consumer Price Index ("Israeli CPI") are adjusted at the relevant index at each reporting date according to the terms of the agreement.

3. Revenue recognition basis

The criteria used by the Bank for recognizing income and expenses in the financial statements are as follows:

- Financial assets and liabilities measured at amortized cost – interest income is recognized using the effective interest method.
- Financial assets and liabilities measured at fair value through profit or loss – income is initially recognized using the effective interest method and subsequently recognized as an adjustment to the fair value of the financial asset.
- Financial assets and liabilities measured at fair value through other comprehensive income – including equity investments, the changes in fair value in the period are carried to other comprehensive income since these are investments that the Bank strongly intends to keep for the long term that are initially designated as such as per IFRS 9.
- Income and expenses from commissions and other income from services are recognized in profit or loss when the services are rendered.

Following are data on the NIS exchange rates against other key currencies:

	December 31,			Rate of change	
	2021	2020	2019	2021	2020
	NIS			Percent	
US Dollar	3.110	3.215	3.456	(3.3)	(7.0)
Euro	3.520	3.944	3.878	(10.8)	1.7
Pound Sterling	4.203	4.392	4.560	(4.3)	(3.7)
Special Drawing Rights (SDRs) ¹	4.409	4.641	4.789	(5.0)	(3.1)

¹The SDR rate published by the IMF is determined according to a weighted basket of five currencies – the US Dollar, Euro, Japanese Yen, Pound Sterling and Chinese Yuan.



C. Indexation

Indexed assets and liabilities in local currency are shown in accordance with the indexation terms determined for each balance. Following are data on the Israeli CPI (based on the 2016 average):

	December 31,			Rate of change	
	2021	2020	2019	2021	2020
	Points			Percent	
For November	103.6	101.2	101.8	2.4	(0.6)
For December	103.9	101.1	101.8	2.8	(0.7)

D. Interest rates

Some of the interest collected or paid by the Bank of Israel is based on the Bank of Israel interest rate or the Prime interest rate.

Following are data on the interest rates:

	December 31,		
	2021	2020	2019
	Percent		
Bank of Israel interest rate	0.10	0.10	0.25
Prime interest rate	1.60	1.60	1.75

E. Cash and cash equivalents

Cash consists of cash that is readily usable and demand deposits.

Cash equivalents are considered as highly liquid investments, including unrestricted short-term bank deposits with an original maturity of three months or less from the date of investment or with a maturity of more than three months, but which are redeemable on demand without penalty and which form part of the Bank's cash management.

F. Short-term deposits

Short-term bank deposits are deposits with an original maturity of more than three months from the date of investment and which do not meet the definition of cash equivalents. The deposits are presented according to their terms of deposit.

G. Fixed assets

Fixed assets are stated at cost with the addition of direct acquisition costs, less accumulated depreciation and accumulated impairment losses and do not include ongoing maintenance expenses.

Improvements and enhancements are charged to the cost of the assets and depreciated over their useful lives, whereas maintenance and repair expenses are charged to profit or loss as incurred.

Depreciation is calculated by the straight-line method based on the estimated useful life of the asset:

- Buildings (excluding the land component)–1.5%-2%;
- Equipment and furniture–10%;
- Vehicles–15%;
- Computers–25%;

The useful life, depreciation method and residual value of an asset are reviewed at least each year-end and any changes are accounted for prospectively as a change in accounting estimate. Depreciation of an asset ceases at the earlier of the date that the asset is classified as held for sale and the date that the asset is derecognized.

H. Intangible assets

Separately acquired intangible assets are measured on initial recognition at cost including directly attributable costs. Expenditures relating to internally generated intangible assets, excluding capitalized development costs, are recognized in profit or loss when incurred.

Intangible assets with a finite useful life are amortized on a straight-line basis over their useful life and reviewed for impairment whenever there is an indication that the asset may be impaired. The amortization period and the amortization method for an intangible asset are reviewed at least at each year end.

The useful life of intangible assets is estimated at 4 years with an annual amortization rate of 25%.

I. Banknotes and coins in circulation

Banknotes and coins in circulation that were issued by the Bank reflect the Bank's liability to their holders. This liability is shown in the Bank's Statement of Financial Position at face value. Expenses of printing banknotes and minting coins are shown in the Statement of Profit or Loss.

J. Financial instruments

1. Financial assets:

Financial assets are measured upon initial recognition at fair value plus transaction costs that are directly attributable to the acquisition of the financial assets, except for financial assets measured at fair value through profit or loss in respect of which transaction costs are recorded in profit or loss.

The Bank classifies and measures debt instruments in the financial statements based on the following criteria:

- a) The bank's business model for managing financial assets; and
- b) The contractual cash flow terms of the financial asset.

a) **Debt instruments are measured at amortized cost when:**

The Bank's business model is to hold the financial assets in order to collect their contractual cash flows, and the contractual terms of the financial assets give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding. After initial recognition, the instruments in this category are measured according to their terms at amortized cost using the effective interest rate method, less any provision for impairment.

On the date of initial recognition, the Bank may irrevocably designate a debt instrument as measured at fair value through profit or loss if doing so eliminates or significantly reduces a measurement or recognition inconsistency, such as when a related financial liability is also measured at fair value through profit or loss.

b) **Debt instruments are measured at fair value through other comprehensive income when:**

The Bank's business model is to hold the financial assets in order to both collect their contractual cash flows and to sell the financial assets, and the contractual terms of the financial assets give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

After initial recognition, the instruments in this category are measured at fair value. Gains or losses from fair value adjustments, excluding interest and exchange rate differences, are recognized in other comprehensive income.

c) **Debt instruments are measured at fair value through profit or loss when:**

A financial asset which is a debt instrument does not meet the criteria for measurement at amortized cost or at fair value through other comprehensive income. After initial recognition, the financial asset is measured at fair value and gains or losses from fair value adjustments are recognized in profit or loss.

d) **Equity instruments and other financial assets held for trading:**

Investments in equity instruments do not meet the above criteria and accordingly are measured at fair value through profit or loss.

Other financial assets held for trading including derivatives are measured at fair value through profit or loss unless they are designated as effective hedging instruments.

In respect of certain equity instruments that are not held for trading, on the date of initial recognition, the Bank made an irrevocable election to present subsequent changes in fair value in Other Comprehensive Income, which changes would have otherwise been recorded in profit or loss. These changes will not be reclassified to profit or loss in the future, even when the investment is disposed of.

Dividends from investments in equity instruments are recognized in profit or loss when the right to receive the dividends is established.

2. Impairment of financial assets

The Bank evaluates at the end of each reporting period the loss allowance for financial debt instruments that are not measured at fair value through profit or loss. The Bank distinguishes between two types of loss allowances:

- a) Debt instruments whose credit risk has not increased significantly since initial recognition, or whose credit risk is low - the loss allowance recognized in respect of this debt instrument is measured at an amount equal to the expected credit losses within 12 months from the reporting date (12-month ECLs); or
- b) Debt instruments whose credit risk has increased significantly since initial recognition, and whose credit risk is not low - the loss allowance recognized is measured at an amount equal to the expected credit losses over the instrument's remaining term (lifetime ECLs).

An impairment loss on debt instruments measured at amortized cost is recognized in profit or loss with a corresponding loss allowance that is offset from the carrying amount of the financial asset, whereas the impairment loss on debt instruments measured at fair value through other comprehensive income is recognized in profit or loss with a corresponding loss allowance that is recorded in other comprehensive income and not as a reduction of the carrying amount of the financial asset in the statement of financial position.

The Bank applies the low credit risk simplification in IFRS 9, according to which the bank assumes the debt instrument's credit risk has not increased significantly since initial recognition if on the reporting date it is determined that the instrument has a low credit risk, for example when the instrument has an external rating of "investment grade".

3. Derecognition of financial assets

A financial asset is derecognized only when the contractual rights to the cash flows from the financial asset have expired.

4. Financial liabilities

a) Financial liabilities measured at amortized cost:

Financial liabilities are initially recognized at fair value less transaction costs that are directly attributable to the issue of the financial liability.

After initial recognition, the Bank measures all financial liabilities at amortized cost using the effective interest rate method, except for:

- Financial liabilities measured at fair value through profit or loss;
- Financial liabilities that arise when a transfer of a financial asset does not qualify for derecognition or when the continuing involvement approach applies;

b) Financial liabilities measured at fair value through profit or loss:

Financial liabilities measured at fair value through profit or loss include derivatives.

After initial recognition, changes in fair value are recognized in profit or loss.

5. Derecognition of financial liabilities

A financial liability is derecognized only when it is extinguished, that is when the obligation specified in the contract is discharged or canceled or expires. A financial liability is extinguished when the debtor discharges the liability by paying in cash, other financial assets, goods or services; or is legally released from the liability.

When there is a modification in the terms of an existing financial liability, the Bank evaluates whether the modification is substantial, taking into account qualitative and quantitative information.

If the terms of an existing financial liability are substantially modified or a liability is exchanged for another liability from the same lender with substantially different terms, the modification or exchange is accounted for as an extinguishment of the original liability and the recognition of a new liability. The difference between the carrying amounts of the above liabilities is recognized in profit or loss.

If the modification in the terms of an existing liability is not substantial or if a liability is exchanged for another liability from the same lender whose terms are not substantially different, the Bank recalculates the carrying amount of the liability by discounting the revised cash flows at the original effective interest rate and any resulting difference is recognized in profit or loss.

6. Offsetting financial instruments

Financial assets and financial liabilities are offset and the net amount is presented in the statement of financial position if there is a legally enforceable right to set off the recognized amounts and there is an intention either to settle on a net basis or to realize the asset and settle the liability simultaneously. The right of offset must be legally enforceable not only during the ordinary course of business of the parties to the contract but also in the event of bankruptcy or insolvency of one of the parties. In order for the right of set-off to be currently available, it must not be contingent on a future event, there may not be periods during which the right is not available, or there may not be any events that will cause the right to expire.



K. Fair value measurement

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

Fair value measurement is based on the assumption that the transaction will take place in the asset's or the liability's principal market, or in the absence of a principal market, in the most advantageous market.

The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

Fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its best use or by selling it to another market participant that would use the asset in its highest and best use.

The Bank uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximizing the use of relevant observable inputs and minimizing the use of unobservable inputs.

All assets and liabilities measured at fair value or for which fair value is disclosed are categorized into levels within the fair value hierarchy based on the lowest level input that is significant to the entire fair value measurement:

Level 1 - quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2 - inputs other than quoted prices included within Level 1 that are observable directly or indirectly.

Level 3 - inputs that are not based on observable market data (valuation techniques which use inputs that are not based on observable market data).

L. Employee benefit liabilities

The Bank has several employee benefit plans:

1. Short-term employee benefits

Short-term employee benefits are benefits that are expected to be settled wholly before twelve months after the end of the annual reporting period in which the employees render the related services. These benefits include salaries, paid annual leave, paid sick leave, recreation and social security contributions and are recognized as expenses as the services are rendered. A liability in respect of a cash bonus or a profit-sharing plan is recognized when the Bank has a legal or constructive obligation to make such payment as a result of past service rendered by an employee and a reliable estimate of the amount can be made.

2. Post-employment benefits

The plans are normally financed by contributions to insurance companies and classified as defined contribution plans or as defined benefit plans.

The Bank has defined contribution plans pursuant to Section 14 of the Severance Pay Law under which the Bank pays fixed contributions and will

have no legal or constructive obligation to pay further contributions if the fund does not hold sufficient amounts to pay all employee benefits relating to employee service in the current and prior periods.

Contributions to the defined contribution plan in respect of severance or retirement pay are recognized as an expense when contributed concurrently with performance of the employee's services.

The Bank also operates a defined benefit plan in respect of pension, severance pay and other benefits to employees insured under budgetary pension and redemption of sick leave. The liability for termination of employment is measured using the projected unit credit method. The actuarial assumptions include expected salary increases and rates of employee turnover based on the estimated timing of payment. The amounts are presented based on discounted expected future cash flows using a discount rate determined by reference to market yields at the reporting date on high quality corporate bonds that are linked to the CPI with a term that is consistent with the estimated term of the severance pay obligation.

The Bank's net obligation for post-employment benefits, which is computed based on actuarial assumptions, is for the future benefit due to the employees for service rendered in the current period and in prior periods and taking into account expected salary increases. The amount of these benefits is discounted to its present value. The discount rate is determined by reference at the reporting date to market yields on government bonds whose term is consistent with the term of the Bank's obligation.

Remeasurements of the net liability are recognized in other comprehensive income in the period in which they occur.

3. Other long-term employee benefits

The Bank's employees are entitled to benefits in respect of paid absences, jubilee grants and adaptation grants. These benefits are accounted for as other long-term benefits since the Bank estimates that these benefits will be used and the respective Bank's obligation will be settled during the employment period and more than twelve months after the end of the annual reporting period in which the employees render the related service. The liability for other long-term employee benefits is measured using the projected unit credit method similarly to the liability for post-employment benefits.

Remeasurements of the net liability are recognized in profit or loss in the period in which they occur.

M. Disclosure of new standards in the period prior to their adoption

1. Annual improvements to IFRSs 2018-2020

In May 2020, the IASB issued certain amendments in the context of the Annual Improvements to IFRSs 2018-2020 Cycle. The main amendment is to IFRS 9, "Financial Instruments" ("the Amendment"). The Amendment clarifies which fees a bank should include in the "10% test" described in paragraph B3.3.6 of IFRS 9 when assessing whether the terms of a debt instrument that has been modified or exchanged are substantially different from the terms of the original debt instrument.

The Amendment is effective for annual periods beginning on or after January 1, 2022. Early application is permitted. The Amendment is to be applied to debt instruments that are modified or exchanged commencing from the year in which the Amendment is first applied.

2. Amendment to IAS 1, "Presentation of Financial Statements"

In January 2020, the IASB issued an amendment to IAS 1, "Presentation of Financial Statements" ("the Amendment") regarding the criteria for determining the classification of liabilities as current or non-current.

The Amendment includes the following clarifications:

- What is meant by a right to defer settlement;
- That a right to defer must exist at the end of the reporting period;
- That classification is unaffected by the likelihood that an entity will exercise its deferral right;
- That only if an embedded derivative in a convertible liability is itself an equity instrument, would the terms of a liability not impact its classification.

The Amendment is effective for annual periods beginning on or after January 1, 2023 and must be applied retrospectively. Early application is permitted

The Bank is evaluating the possible impact of the Amendment on its current loan agreements.



3. Amendment to IAS 8, "Accounting Policies, Changes to Accounting Estimates and Errors"

In February 2021, the IASB issued an amendment to IAS 8, "Accounting Policies, Changes to Accounting Estimates and Errors" ("the Amendment"), in which it introduces a new definition of "accounting estimates".

Accounting estimates are defined as "monetary amounts in financial statements that are subject to measurement uncertainty". The Amendment clarifies the distinction between changes in accounting estimates and changes in accounting policies and the correction of errors.

The Amendment is to be applied prospectively for annual reporting periods beginning on or after January 1, 2023 and is applicable to changes in accounting policies and changes in accounting estimates that occur on or after the start of that period. Early application is permitted.

The Bank is evaluating the effects of the Amendment on its financial statements.

N. Taxes

According to the Bank of Israel Law, regarding the payment of taxes, municipal taxes, levies and other mandatory payments, the Bank has the same status as the State of Israel. In addition, regarding the taxation of the Bank's global investments, the Bank is tax exempt on most of its investments in foreign securities. The tax expenses charged to the Bank on its global investments are shown in the Statement of Profit or Loss in the "Miscellaneous expenses, net" line item.

O. Significant accounting judgments, estimates and assumptions used in the preparation of the financial statements

In the process of applying the significant accounting policies, the Bank has made the following judgments which have the most significant effect on the amounts recognized in the financial statements:

1. Evaluating the business model

The Bank evaluates the objective of the business model according to which financial assets are held in a portfolio since it optimally reflects the method of managing the assets and the communication of information to Management. The information taken into account consists of:

- The objective of holding the portfolio for trade, for generating contractual cash flows etc.;
- The frequency, value and timing of sales (both in the past and in the future);
- The method of evaluating and reporting the performances of the business model and financial assets to key management personnel in the Bank;

- The risks affecting the business model performances and their management;
- The method of remuneration of investment managers. For example, is the remuneration based on the fair value of the managed assets or on the contractual cash flows received;
- Whether the contractual cash flows received (such as interest income) represent a significant portion of the portfolio returns.

2. Calculation of the allowance for expected credit losses

The Bank evaluates the allowance for expected credit losses (ECLs) in respect of the entire instruments measured at amortized cost or of debt instruments measured at fair value through other comprehensive income (FVTOCI). ECLs are calculated based on the following formula: $ECL = PD * LGD * EAD$.

- a) PD = probability of default (%) is the likelihood over a specified period that a borrower will not be able to make scheduled repayments. PD is estimated for a specific date based on statistical rating models using rating tools that are adapted to the various counterparty and exposure categories. The PD for foreign counterparties within a period of one year relies on Bloomberg's Default Risk (DRSK) models for corporations and Bloomberg's sovereign risk function (SRSK) using financial, macroeconomic and credit score data.
- b) LGD = loss given default (%) is the estimated loss in the event of default on a loan based on the difference between the cash flows receivable as per the contract and cash flows the lender expects to actually receive, also given the cash flows that may be received from collaterals. The LGD relies on the default recovery rate (RR).
- c) EAD = exposure at default of a financial asset calculated as the gross carrying amount (including accrued interest).

3. Employee benefits

See Note 9a for the principles underlying the actuarial calculation.

4. Fair value

See Note 12 for the fair value measurement techniques.



NOTE 3 | FOREIGN EXCHANGE RESERVES

As per the Bank of Israel Law, the Bank is charged with holding and managing the State's foreign exchange reserves and supporting the regular operation of the Israeli foreign exchange market.

Foreign exchange reserves are foreign currency assets and liabilities held by the Bank of Israel outside of Israel for the purpose of performing the Bank's duties.

Foreign exchange reserves are invested in various financial instruments, most of which are internally managed by the Bank and some that are managed externally, all in the context of the investment policy outlined by the Monetary Committee.

Below is the composition of foreign exchange reserves according to investment type:

	Note	December 31,	
		2021	2020
		NIS million	
Cash and cash equivalents	3a	170,870	132,735
Securities (a)			
Government, multinational and public sector bonds		302,348	276,001
Corporate bonds		38,324	31,458
Commercial securities		23,927	30,515
Mortgage-backed securities		9,266	9,725
Shares		115,475	73,226
Total securities		489,340	420,925
Other assets (b)			
Short-term deposits	3b1	3,240	8,966
Various assets	3b2	539	3,417
Total other assets		3,779	12,383
The IMF (b)	3c	14,534	6,606
Other liabilities (b)			
Securities purchased in repo agreements		(16,754)	(11,811)
Various liabilities		(1,681)	(96)
Total other liabilities		(18,435)	(11,907)
Derivative financial instruments (a)	3d		
Assets		2,665	466
Liabilities		(345)	(4,042)
Total derivative financial instruments		2,320	(3,576)
Total foreign exchange reserves		662,408	557,166



Financial instrument measurement categories:

- a. Financial assets/liabilities measured at fair value through profit or loss.
- b. Financial assets/liabilities measured at amortized cost.

Below is the composition of foreign exchange reserves according to currency type at each year end:

	December 31,	
	2021	2020
	Percent	
USD	64.9	65.6
Euro	28.6	28.4
Pound Sterling	2.7	2.6
Other	3.8	3.4
Total	100	100

NOTE 3a | CASH AND CASH EQUIVALENTS

Below is the composition of the Bank's cash and cash equivalents:

	December 31,	
	2021	2020
	NIS million	
Demand deposits in central banks	170,635	126,643
Demand deposits used for external management	235	142
Foreign currency deposits ¹	-	5,950
Total cash and cash equivalents	170,870	132,735

¹ Deposits in central banks whose maturity is less than three months from the investment date.

The annual interest rates on demand deposits range between 0.35 percent and 1.3 percent (in 2020 – same).

As of December 31, 2020, the interest rate on time deposits in central banks which mature within three months was 0.22 percent.

NOTE 3b | OTHER ASSETS AND LIABILITIES ABROAD

1. This item consists of time deposits in central banks or financial institutions whose original maturity exceeds three months from the investment date and which do not meet the criteria of cash equivalents. The deposits are stated at their amortized cost based on their deposit terms. The annual interest rates on these deposits range between 0.62 percent and 0.58 percent (in 2020 – between 0.08 percent and 0.35 percent).



2. This item mainly consists of collaterals which are provided by the Bank or provided in favor of the Bank vis-à-vis different financial institutions, in accordance with the Bank's exposure to derivative financial instruments (when the collaterals are provided in favor of the Bank, they are stated in liabilities) and restricted cash used to secure forwards and derivative transactions. The restricted cash is shown in accordance with its terms of deposit.

NOTE 3c | THE INTERNATIONAL MONETARY FUND (IMF)

In accordance with Section 82 to the Bank of Israel Law, "Representing the State vis-à-vis International Financial Institutions", the Bank represents the State in the IMF.

The IMF created an international reserve asset known as Special Drawing Rights ("SDRs"). The entire operations, assets and liabilities in respect of the IMF are denominated in SDR. The SDR rate is published by the IMF and calculated based on a weighted currency basket that includes the USD, the Euro, the Japanese Yen, the Pound Sterling and the Chinese Yuan. The IMF is considered a senior creditor.

Below is the concentration of assets and liabilities in the IMF:

	December 31,		December 31,	
	2021	2020	2021	2020
	NIS million		SDR million	
IMF quota	8,469	8,914	1,921	1,921
NAB loans	35	76	8	16
SDRs	12,233	4,145	2,775	893
Total IMF assets	20,737	13,135	4,704	2,830
Deposits	(897)	(944)	(204)	(204)
Bank notes	(5,306)	(5,585)	(1,203)	(1,203)
Total IMF liabilities in local currency	(6,203)	(6,529)	(1,407)	(1,407)
IMF balance	14,534	6,606	3,297	1,423
Allocated SDRs	(12,013)	(4,100)	(2,725)	(884)
Total IMF balance¹	2,521	2,506	572	539

¹ The balances bear interest pursuant to the IMF's terms. As of December 31, 2021, the interest rate is 0.077 percent (as of December 31, 2020 – 0.08 percent).

Assets and liabilities in the IMF

a. IMF quota

Each member country of the IMF has a quota for its participation in the Fund's capital, a quota which is denominated in SDR. The IMF quota determines the maximum amount of financial resources that the member country is obligated to provide the IMF. A country pays 25% of its quota in standard foreign currencies or in SDRs and the remaining 75% in its own currency. The part of the quota that is paid in cash may be withdrawn by the country, whereas the rest is deposited with the country's central bank in deposits and notes indexed to SDR (see paragraphs e and f below). The quota defines the member country's voting power in IMF resolutions. As of December 31, 2021, the State of Israel has 20,668 votes on the IMF accounting for 0.41 percent of total votes (unchanged from December 31, 2020). The State of Israel has been a member of the IMF since July 12, 1954.

b. NAB loans

From September 2010, the State of Israel has been part of the IMF's credit arrangement known as NAB (New Arrangements to Borrow). In accordance with this arrangement, member countries, including Israel, provide a credit line to the IMF, in the context of which loans are extended with maturities of ten years. According to the arrangement, the loans may be repaid to each country at an earlier date, at the country's request, should it need the money.

On January 1, 2021, a renewed NAB became effective according to which the credit line provided by member countries to the IMF was doubled with the countries' consent. As of December 31, 2021, the maximum credit line that the Bank of Israel provides the IMF is SDR 680 million (NIS 2,998 million) (as of December 31, 2020, the maximum credit line that the Bank of Israel provided the IMF was about SDR 340 million (NIS 1,578 million)). Since any potential claim is filed against the IMF itself, the State is not exposed to any third party claims in connection with NAB loans.

c. Special Drawing Rights (SDRs)

SDRs are reserve assets that are equivalent to foreign currency that are allocated by the IMF to the member countries pro rata to their quota. The value of SDRs as reserve assets derives from the member countries' obligation to hold and receive SDRs and honor various commitments relating to the operation of this system. The IMF member countries may exchange the reserves against foreign currency.

The balance bears interest at the IMF's terms. In the reporting year, the IMF allocated Israel about SDR 1.8 million as part of the overall allocations to member countries which totalled about \$650 billion in order to increase global reserves, build trust, promote the stability of the global economy and particularly assist underprivileged countries in dealing with the economic



ramifications of the COVID-19 pandemic. Concurrently with the increase in the IMF's assets, a long-term liability to the IMF was recorded in the allocated amount (see paragraph f below).

d. Deposits

Deposits are comprised of two types: (1) deposits used for IMF transactions and operations (such as membership fees, purchases, repurchases, loan repayment and NIS sales); and (2) deposits used for IMF related general and administrative expenses in local currency and within the State's jurisdiction. These deposits are denominated in local currency and indexed to the SDR rate as published by the IMF.

e. Bank notes

Bank notes issued by the Bank against the increase of the IMF quota for participation in the IMF's equity. These notes are denominated in local currency and indexed to the SDR rate as published by the IMF.

f. Allocated SDRs

These represent member countries' purchase commitments to the IMF. The commitments do not have a maturity date and they bear interest at the IMF's terms. The IMF allocates its member countries SDRs pro rata to their quota. The Bank's balance at the IMF is measured at amortized cost and revalued to the SDR rate published by the IMF. Exchange rate revaluation gains and losses from the revaluation of IMF assets and liabilities are carried to profit or loss.

NOTE 3d | DERIVATIVE FINANCIAL INSTRUMENTS

This item consists of foreign currency transactions such as spots, gross settled forwards, net settled non-deliverable forwards (NDFs) and currency swaps, all of which are included in the Statement of Financial Position from the date of entering into such transactions. The Bank pays or receives collaterals in respect of some of these transactions (see Note 3b above).

NOTE 4 | BIS INVESTMENT

In accordance with Section 82 of the Bank of Israel Law, the Bank represents the State of Israel vis-à-vis the Bank for International Settlements ("BIS"). BIS is an international organization of central banks designed to cultivate international currency and financial collaborations and serve as a bank for all central banks. The Bank of Israel holds 3,211 shares in the BIS at a value of about NIS 398 million as of December 31, 2021 (as of December 31, 2020 – about NIS 399 million). The shares are held as part of the Bank's duties as a central bank and naturally have long positions. Each shareholder is entitled to receive its share of BIS's NAV with a 30%



discount. BIS shares can only be transferred with BIS's advance consent. The Bank of Israel has no intention to sell its BIS shares.

The Bank calculates the fair value of the investment pro rata to its share of BIS' capital less 30%. The 30% is deducted for repurchases of shares made by BIS from 1970s and due to the decision of the Hague Court of Appeal from 2001.

The Bank classifies the BIS investment as a strategic investment and therefore changes in its fair value are recognized in other comprehensive income and accumulate in the equity revaluation reserve as per IFRS 9. Dividends are recognized in the Statement of Profit or Loss since they represent a return on capital and not a return of the invested capital to the shareholders.

NOTE 5 | LOCAL FINANCIAL INSTRUMENTS

	December 31, 2021	
	Carrying amount	Average interest rate
	NIS million	Percent
Assets:		
Local currency bonds (a)		
Government bonds	83,630	0.063%
Corporate bonds	3,024	0.13%
	86,654	
Loans to financial institutions		
Loans to banking corporations (b)	40,028	-0.1%, 0.1%
Securities purchased in reverse repo agreements (c)	100	0.1%
	40,128	
Liabilities:		
Reserves of banking corporations against reserve requirement (d)		
Local currency reserves	73,582	-
Foreign currency reserves – foreign currency deposits	7,886	-
	81,468	
Monetary absorption tools		
Time deposits (e)	474,005	0.1%
Short-term bills (<i>makam</i>) (f)	114,984	0.03%
	588,989	
Government reserves (g)		
Local currency reserves	44,053	0.6%
Foreign currency reserves	5,669	0.06%
	49,722	



	December 31, 2020	
	Carrying amount	Average interest rate
	NIS million	Percent
Assets:		
Local currency bonds (a)		
Government bonds	46,995	0.12%
Corporate bonds	3,350	0.13%
	50,345	
Loans to financial institutions		
Loans to banking corporations (b)	19,564	-0.1%,0.1%
Securities purchased in reverse repo agreements (c)	1,497	0.1%
	21,061	
Liabilities:		
Reserves of banking corporations against reserve requirement (d)		
Local currency reserves	53,499	-
Foreign currency reserves – foreign currency deposits	1,518	-
	55,017	
Monetary absorption tools		
Time deposits (e)	365,002	0.13%
Short-term bills (<i>makam</i>) (f)	86,975	0.08%
	451,977	
Government reserves (g)		
Local currency reserves	41,456	0.96%
Foreign currency reserves	6,169	0.41%
	47,625	

Details of local financial instruments:

- a. **Local currency bonds** – local currency government and corporate bonds. In March 2020, the Bank launched several plans for buying government bonds on the secondary market in order to facilitate market credit terms and support economic activity and financial stability in the market. The plans were concluded at the end of 2021.

In July 2020, due to aggravated economic conditions in Israel, the Bank initiated a plan for buying corporate bonds by up to NIS 15 billion to expand the financial aid to the market in response to the credit needs. These purchases ended in early 2021.

The bonds consist of government and corporate bonds that are indexed to the known Israeli CPI as of the balance sheet date and unindexed government and corporate bonds.

The bonds are stated at amortized cost subject to impairment.

The carrying amount of the investment in corporate bonds as of December 31, 2021 includes an allowance for ECLs totaling about NIS 3 million



(December 31, 2020 – about NIS 4 million), which reduced the carrying amount of the investment and was carried to the Statement of Profit or Loss.

The credit ratings of local currency corporate bonds:

Corporate bonds					
December 31, 2021					
	AAA	AA+,AA,AA-	A+,A,A-	BBB+	Total
NIS million	642	1,663	718	1	3,024
Percent	21%	55%	24%	0%	100%

December 31, 2020					
	AAA	AA+,AA,AA-	A+,A,A-	BBB+	Total
NIS million	663	1,847	839	1	3,350
Percent	20%	55%	25%	0%	100%

- b. **Loans to banking corporations** – loans granted to banking corporations in an aim to increase the scope of bank credit offerings to small and micro businesses as a COVID-19 financial relief program. The Bank of Israel receives collaterals from the banking corporations against the loans. The loans are granted for periods of 3 or 4 years and bear interest at rates of 0.1 or -0.1 percent a year, which is paid at the end of the loan period as per the published decisions of the Monetary Committee.

According to the Bank's evaluations, the value of the loans does not exceed the value of the collaterals and therefore no allowance is recorded for ECLs.

- c. **Securities held as per reverse repurchase (r.repo) agreements** – in March 2020, the Bank began buying government bonds, corporate bonds or short-term bills (*makam*) from institutional investors and mutual funds subject to future sale (r. repo) agreements. These purchases were designed to improve liquidity in the financial markets in which the financial institutions operate. The r. repos were signed for a period of one week or one month and bear BOI interest.
- d. **Reserves of banking corporations against reserve requirement** – they represent demand deposits of banking corporations in local currency and in foreign currency (dollar) and are used as liquid assets against deposits of Israeli or foreign residents in accordance with the respective reserve requirements. The reserve requirements depend on the deposit type: 6 percent on time deposits, 3 percent on week to year deposits and no reserve requirement for deposits over a year. The Bank of Israel does not pay the banking corporations interest on the reserve requirements or on excess reserves.
- e. **Time deposits** – the Bank of Israel receives from the banking corporations time deposits in NIS as per Section 36(3) of the Bank of Israel Law. The deposits are received via auction for periods of one day, one week and reserve periods.



The deposits are not used as a liquid asset against the banking corporations' reserve requirement.

As of December 31, 2021, the average interest rate on time deposits is 0.1 percent (December 31, 2020 – 0.1 percent). In 2021, the average interest rate on auction time deposits was 0.1 percent (2020 – 0.13 percent).

As of December 31, 2020, the interest rate on deposits at the deposit window was 0 percent (December 31, 2020 – 0 percent).

- f. **Short-term bills (*makam*)** – these are securities auctioned to the public by the Bank of Israel as one of the monetary tools used by the Bank. The bills are issued for a maximum period of one year, are unindexed and interest free. They are sold and traded at a discount for a price lower than their face value and presented in the financial statements at amortized cost.
- g. **Government reserves** – they comprise the Government's local currency and foreign currency reserves held by the Bank and can be offset against each other, except for certain irregular reserves.
 - 1. Government reserves in local currency consist of current balances and balances used for lending bonds for financing budget operations. For current credit and debit balances, the Bank of Israel respectively charges or pays the Government interest ranging between BOI interest + 1.5 percent and BOI interest at various brackets. Government reserves which are used for lending bonds and other balances are subject to different interest.
 - 2. Government reserves in foreign currency mainly consist of current balances used for financing the budget operations. Some of these balances are subject to interest at the rate of the interest on U.S. Treasury notes with average maturity of 6 months.



NOTE 6 | OTHER LOCAL ASSETS

	December 31,	
	2021	2020
	NIS million	
Credit to the Government (1)	103	106
Loans to employees	89	79
Various receivables	8	3
Total other assets	200	188

(1) This line item consists of credit extended to the Israeli Government for joint investment with the U.S. Government in binational industrial and scientific R&D foundations which are mainly denominated in USD.

The binational foundations deposit the amounts in the Bank of Israel and they are stated in the Statement of Financial Position under local liabilities in the line item "other local currency liabilities".

The credit and deposits bear fixed interest of 4 percent and 4.125 percent, respectively and are indexed to the CPI or Libor based.

NOTE 7 | Fixed assets and Intangible assets

Below is the composition of the balances and changes therein for 2021:

	Land and buildings ¹	Equipment, furniture and vehicles ²	Computers and electronic equipment ²	Total	Intangible assets ²	Total
	NIS million					
Cost:						
Balance as of January 1, 2021	600	111	435	1,146	261	1,407
Additions in the year	14	4	10	28	39	67
Disposals in the year	(1)	(4)	(6)	(11)	-	(11)
Balance as of December 31, 2021	613	111	439	1,163	300	1,463
Accumulated depreciation:						
Balance as of January 1, 2021	100	61	252	413	171	584
Additions	11	7	56	74	31	105
Disposals	-	(3)	(6)	(9)	-	(9)
Balance as of December 31, 2021	111	65	302	478	202	680
Depreciated balance as of December 31, 2021	502	46	137	685	98	783
Depreciated balance as of December 31, 2020	500	50	183	733	90	823

¹ The cost of the Bank's property in the Jerusalem Campus and the depreciated cost of the buildings thereon, amount to approximately NIS 472 million as of December 31, 2021 (approximately NIS 479 million as of December 31, 2020). The Bank is not registered as the lessee of the Bank's properties. The lease expired on June 30, 2016. Since then, the Bank has been negotiating the renewal of the lease agreement with the Israel Land Authority (the ILA).



Accordingly, the Bank may be required to pay lease fees when the lease is renewed. At this stage, the Bank is unable to assess when the ILA will renew the lease agreement with the Bank and whether the renewal will consist of any charge and therefore, as of the financial statement publication date, no provision was recorded.

² In 2019, the Bank began operating a credit data system which was designed in accordance with the Credit Data Law, 5776-2016, to help increase competition in the Israeli retail credit market. The depreciated cost of the credit data system as of December 31, 2021 was about NIS 99 million (December 31, 2020 – about NIS 141 million).

Below is the composition of the balances and changes therein for 2020:

	Land and buildings ¹	Equipment, furniture and vehicles ²	Computers and electronic equipment ²	Total	Intangible assets ²	Total
	NIS million					
Cost:						
Balance as of January 1, 2020	553	113	427	1,093	236	1,329
Additions in the year	47	8	15	70	25	95
Disposals in the year	-	(10)	(7)	(17)	-	(17)
Balance as of December 31, 2020	600	111	435	1,146	261	1,407
Accumulated depreciation:						
Balance as of January 1, 2020	93	61	200	354	142	496
Additions	7	7	58	72	31	103
Disposals	-	(9)	(6)	(15)	-	(15)
Balance as of December 31, 2020	100	59	252	411	173	584
Depreciated balance as of December 31, 2020	500	52	183	735	88	823
Depreciated balance as of December 31, 2019	460	52	227	739	94	833

¹ The cost of the Bank's property in the Jerusalem Campus and the depreciated cost of the buildings thereon, amount to approximately NIS 479 million as of December 31, 2020 (approximately NIS 436 million as of December 31, 2019). The Bank is not registered as the lessee of the Bank's properties. The lease expired on June 30, 2016. Since then, the Bank has been negotiating the renewal of the lease agreement with the Israel Land Authority (the ILA). Accordingly, the Bank may be required to pay lease fees when the lease is renewed. At this stage, the Bank is unable to assess when the ILA will renew the lease agreement with the Bank and whether the renewal will consist of any charge and therefore, as of the financial statement publication date, no provision was recorded.

² In 2019, the Bank began operating a credit data system which was designed in accordance with the Credit Data Law, 5776-2016, to help increase competition in the Israeli retail credit market. The depreciated cost of the credit data system as of December 31, 2020 was about NIS 141 million (December 31, 2019 – about NIS 192 million).



NOTE 8 | BANKNOTES AND COINS IN CIRCULATION

This line item represents the balance of banknotes and coins in circulation held by the public. The liability in their respect is presented in the Bank's Statement of Financial Position at face value.

The liability for issued banknotes and coins is presented in a net amount after offsetting the banknotes and coins held by the Bank. Following are details of banknotes and coins in circulation:

	December 31,	
	2021	2020
	NIS million	
NIS 20	1,126	1,050
NIS 50	3,731	3,527
NIS 100	18,274	18,106
NIS 200	87,073	80,444
Coins in circulation	2,866	2,670
Commemorative banknotes and coins	6	6
Other ¹	2	2
Total banknotes and coins in circulation	113,078	105,805

¹ Special coin items in circulation.

NOTE 9 | OTHER LOCAL LIABILITIES

	December 31,	
	2021	2020
	NIS million	
Liabilities for benefits to employees and pensioners (a)	7,257	6,929
Liabilities for employees' and other rights (b)	44	73
Other payables ¹	1,515	1,406
Total other liabilities	8,816	8,408

¹ The balance mainly comprises accounts of statutory entities that are managed at the Bank of Israel.



A. Liabilities for benefits to employees and pensioners

Employee benefits consist of short-term benefits, post-employment benefits and other long-term benefits, as explained in Note 2 above.

The liability mainly consists of actuarial obligations in respect of post-employment benefits to employees and pensioners. Post-employment benefits to employees and pensioners include payments of future annuities to Bank employees who are recognized by the Bank as budgetary pension insureds, retirement grants and other post-employment benefits, all in keeping with the pension agreement signed with the Bank's employees, pensioners and their survivors.

The Bank's obligation to pay pension and severance to employees who are not insured under budgetary pension is covered by regular deposits to a recognized pension and severance pay fund on behalf of the individual employee. The sums deposited in said manner are neither controlled nor managed by the Bank.

a. Post-employment benefits

1. Defined contribution plans

Section 14 to the Severance Pay Law, 1963 applies to part of the compensation payments, pursuant to which the fixed contributions paid by the Bank into pension funds and/or policies of insurance companies release the Bank from any additional liability to employees for whom said contributions were made. These contributions and contributions for benefits represent defined contribution plans.

	Year ended December 31,	
	2021	2020
	NIS million	
Expenses in respect of defined contribution plans	28	25

2. Defined benefit plans

The Bank accounts for that part of the payment of compensation that is not covered by contributions in defined contribution plans, as above, as a defined benefit plan for which an employee benefit liability is recognized.



Changes in the defined benefit obligation and fair value of plan assets:

2021

	Balance as of January 1, 2021	Expenses recognized in profit or loss				Payments NIS millions	Gain (loss) from remeasurement in other comprehensive income			Balance as of December 31, 2021
		Current service cost	Net interest expense	Past service cost and effect of settlements	Total expense recognized in profit or loss for the period		Actuarial loss arising from changes in financial assumptions	Actuarial gain arising from experience adjustments	Total effect on other comprehensive income for the period	
Defined benefit obligation	6,929	97	105	18	220	(323)	444	(13)	431	7,257

2020

	Balance as of January 1, 2020	Expenses recognized in profit or loss				Payments NIS millions	Gain (loss) from remeasurement in other comprehensive income			Balance as of December 31, 2020
		Current service cost	Net interest expense	Past service cost and effect of settlements	Total expense recognized in profit or loss for the period		Actuarial loss arising from changes in financial assumptions	Actuarial gain arising from experience adjustments	Total effect on other comprehensive income for the period	
Defined benefit obligation	6,916	91	114	3	208	(318)	234	(113)	121	6,929

**b. The principal assumptions underlying the defined benefit plan**

	December 31,	
	2021	2020
	Percent	
Discount rate ¹	0.76-2.079	0.94-1.56
Expected rate of salary increase	1.89-4.81	1.89-4.81
	Years	
	14	14.1
Expected life of the obligation		

¹ The discount rate is based on the interest curve of Israel Government bonds.

c. Amount, timing and uncertainty of future cash flows:

Below are reasonably possible changes at the end of the reporting period in each actuarial assumption assuming that all other actuarial assumptions are constant:

Assumption	Type of change	Percent of change	Type of effect	Percent of effect
Discount interest	Increase (add)	1	Decrease	12.18
Discount interest	Decrease (less)	1	Increase	15.17
Expected rate of salary increase	Increase (times)	20	Increase	0.66
Expected rate of salary increase	Decrease (times)	20	Decrease	0.63
Early retirement	Increase (times)	20	Increase	0.27
Early retirement	Decrease (times)	20	Decrease	0.30
Mortality	Increase (times)	20	Decrease	5.51
Mortality	Decrease (times)	20	Increase	6.98

B. Liabilities for employees' and other rights

This item includes liabilities for salary and other expenses, the majority of which are expected to be settled in the course of 2022.

NOTE 10 | BANK'S EQUITY (DEFICIT) AND RESERVES

	See	December 31,	
		2021	2020
		NIS million	
Bank's equity			
Bank's equity and general reserve	10a	3,985	3,985
Accumulated deficit	10b	(103,662)	(74,262)
		(99,677)	(70,277)
Revaluation reserves	10c		
Equity instruments designated to fair value through other comprehensive income	10c(a)(1)	116	117
Remeasurement of defined benefit plan	10c(a)(2)	(3,538)	(3,107)
Unrealized exchange rate differentials on foreign currency balances	10c(b)(1)	65	2,431
Unrealized gains from fair value adjustments of:	10c(b)(2)		
Bonds		2,974	6,847
Shares		36,561	20,821
Derivative financial instruments		(16)	218
		36,162	27,327
Total Bank's equity (deficit) and reserves		(63,515)	(42,950)

A. The Bank's equity and general reserve

The Bank's equity in historical nominal values as of December 31, 2021 and 2020 was NIS 60 million and the general reserve—NIS 260 million. The general reserve served in the past to increase the Bank's capital in accordance with Section 6 of the Bank of Israel Law, 5714-1954.

The Bank's equity and general reserve in reported amounts after adjustment to the CPI of December 2003 is NIS 3,985 million.

B. Accumulated deficit

Net gains or losses as defined in the Bank of Israel Law which are not distributed to the Government are carried to retained earnings or accumulated deficit (see Note 24 on distributable profits).

C. Revaluation reserves

Revaluation reserves consist of gains (losses) accumulated from the revaluation or remeasurement of items (assets or liabilities) that are recognized as per IFRS as other comprehensive income as well as accumulated unrealized gains from revaluation of items included in net income.



(a) Revaluation reserves recognized against other comprehensive income

These amounts are carried as per IFRS to capital reserves from revaluation of assets or liabilities.

(1) **Revaluation reserve from equity instruments designated to fair value through other comprehensive income**

The Bank made an irrevocable choice to classify its investment in BIS as a strategic share investment that is measured at fair value through other comprehensive income. Gains and losses arising from changes in share prices or from exchange rate revaluation are carried to other comprehensive income under this reserve. These amounts are not reclassified when part of the investment is carried to gains. The relative part of the reserve is reclassified from the reserve to retained earnings.

(2) **Revaluation reserve from remeasurement of defined benefit plan**

Remeasurements of the Bank's defined benefit plan consist of adjustments to actuarial assumptions. They are recognized in other comprehensive income under this reserve. They are not subsequently recognized in profit or loss.

(b) Reserves from revaluation gains included in income (loss) for the year

These revaluation reserves consist of unrealized gains from exchange rate differentials on foreign currency balances and gains from revaluation of financial instruments in foreign currency to fair value. These gains are included in the Bank's annual income (loss) but according to the Bank of Israel Law are not included in distributable net income and therefore they are carried to revaluation reserves until they are actually realized.

(1) **Revaluation reserve from unrealized gains from exchange rate differentials on foreign currency balances**

The Bank recognizes gains and losses from exchange rate differentials in the Statement of Profit or Loss (other than assets measured at fair value through other comprehensive income). In keeping with the Bank's duty to manage foreign exchange reserves for implementing the monetary policy and securing financial stability, the Bank holds unhedged foreign currency balances.

As per the Bank of Israel Law, unrealized gains are not included in distributable net income. The revaluation of exchange rate differentials is not viewed as realization until the currency balance is partially or fully written down. The amount recognized as realized is calculated at the selling rate as opposed to the weighted average cost of buying the foreign currency. Realized gains or losses from exchange rate differentials are carried to retained earnings or accumulated deficit and can be distributed.

The calculation of realized gains is made separately for each currency and foreign currency balances. No offsetting among different types of

items is carried out. The balance of an accumulated loss on a certain currency, if any, is not carried to the revaluation reserve.

(2) **Revaluation reserve from unrealized gains from fair value adjustments**

This reserve comprises gains from fair value changes of financial instruments measured at fair value through profit or loss. When these instruments are sold or derecognized, the accumulated gain or loss previously recognized is reclassified to retained earnings or accumulated deficit.

The calculation is made separately for each security and balances of different assets are not inter-offsetable. The balance of an accumulated loss on a security, if any, is not carried to the revaluation reserve.

NOTE 11 | RISK MANAGEMENT

The Bank's activities expose it to various types of risks such as credit risk, liquidity risk, concentration risk and market risks (interest and currency). Similarly to other central banks, the Bank's activities also expose it to operational risk. As specified in the Bank of Israel Law, the Bank of Israel has objectives and functions that dictate its activities and risk management policy. The Bank's financial results derive from the Bank's risk management policy. The Bank's financial risks can mainly be attributed to managing foreign exchange reserves and conducting transactions in the local market.

As per the Bank of Israel Law, the Bank is charged with holding and managing the State's foreign exchange reserves. Holding foreign exchange reserves provides countries sufficient foreign currency that can be used in the market during a crisis or emergency (such as during a war or natural disaster). The foreign exchange reserves also allow central banks to intervene in the foreign exchange market when needed.

To fulfill these functions, the Monetary Committee, which is headed by the Governor and also consists of representatives from among the public, in consultation with the Minister of Finance, outlines the guidelines for the reserve investment policy and monitors its implementation. The guidelines delineate the investment policy objectives and risk management framework. The specify the types of assets that can be invested in, the risk profile and quantitative and qualitative limitations on the types of assets that can be invested.⁵

The Markets Department is in charge of implementing the policy set forth by the Monetary Committee based on the authorities assigned to the Committee members and the degrees of freedom determined by the Committee.

The Department's investment committee is in charge of supervising and applying means for monitoring financial risks to ascertain that the Bank's activities are

⁵ See more information in the report of foreign exchange reserve investments for 2021.



commensurate with the risk profile and degrees of management freedom outlined by the committee.

The Risk Management Unit in the Markets Department is in charge of regularly monitoring financial risk management and compliance by adopting risk identification, measurement, management and reporting principles and methodologies.

The Markets Department reports the financial and other risks to which the Bank is exposed in respect of foreign exchange reserves to the Monetary Committee on a monthly or quarterly basis.

Monetary policy and financial stability measures are applied in the local market mainly using financial instruments such as government bonds, corporate bonds and loans to banking corporations and financial institutions.

The Markets Department is in charge of monitoring and applying tools for mitigating risks such as requiring proper collaterals for local loans.

1. **Credit risk**

Credit risk is the risk that a counterparty to a financial instrument transaction will not meet its obligations, leading to a loss to the Bank. The Bank is mainly exposed to credit risk from investments in debt instruments for managing foreign exchange reserves. There is also a certain credit risk arising from debt instruments used in the Bank's local activities, but it is assessed as very low.

Foreign exchange reserves

The Bank manages its credit risk exposure by setting specific investment rules and a system of quotas for countries, issuers and banks which is updated annually or as needed. The rules are governed by a regulated methodology that relies on credit ratings, liquidity, product level, market depth, equity and other parameters that apply to the specific country, issuer or bank.

The rules determine credit risk exposure quotas for countries, financial institutions (brokers, banks and international institutions) and issuers. They also prescribe concentration limitations and minimum credit ratings based on international rating agencies.

Future FX and repo transactions are backed by collaterals under daily margins based on market price fluctuations.

The credit portfolio is also diversified using different instruments in the financial market such as fixed interest and variable interest bonds (government, public sector and multinational bonds) and other liquid securities.

Guidelines have been created for managing exceptions to rules and violations of investment rules.



Local market activity

Assets denominated in local currency are mainly used to apply the monetary policy and consist of loans to financial institutions and government and corporate bonds.

The main objective of the Bank's local activities is to implement its monetary policy and therefore the Bank's credit risks in respect of assets denominated in local currency are managed under the policy's requirements.

In respect of loans to financial corporations, the Bank minimizes credit risk using collaterals that consist of central bank deposits and high quality securities placed in the bank such as notes issued by the Government or by corporations. The value of the security underlying each transaction cannot be lower than the value of the loan plus a certain margin. If the value of the security falls below the predetermined level, the Bank requires the counterparty to produce other collaterals based on the revaluation of the securities.

(a) Credit quality analysis

The following tables present a breakdown of the credit ratings of debt assets in the Bank's foreign exchange reserves per type of instrument and currency. The classification into external credit ratings relies on credit ratings published by Moody's.

	December 31, 2021				
	NIS million				
	AAA	AA	A	BBB	Total
Cash and cash equivalents	165,207	3,237	2,426	-	170,870
Government, multinational and public sector bonds	188,407	81,602	30,925	1,414	302,348
Corporate bonds	287	2,343	20,501	15,193	38,324
Commercial securities	8,420	12,821	-	2,686	23,927
Mortgage-backed securities	9,266	-	-	-	9,266
Total	371,587	100,003	53,852	19,293	544,735



December 31, 2021					
NIS million					
	AAA	AA	A	BBB	Total
USD	188,914	10,481	15,703	9,818	224,916
Euro	156,150	52,101	7,275	9,475	225,001
Other	26,523	37,421	30,874	-	94,818
Total	371,587	100,003	53,852	19,293	544,735

December 31, 2020						
NIS million						
	AAA	AA	A	BBB	Lower rating	Total
Cash and cash equivalents	87,849	18,196	26,690	-	-	132,735
Government, multinational and public sector bonds	202,092	61,663	12,246	-	-	276,001
Corporate bonds	622	2,306	12,474	16,046	10	31,458
Commercial securities	13,714	14,325	2,476	-	-	30,515
Mortgage-backed securities	9,725	-	-	-	-	9,725
Total	314,002	96,490	53,886	16,046	10	480,434

December 31, 2020						
NIS million						
	AAA	AA	A	BBB	Lower rating	Total
USD	162,121	14,270	12,073	9,246	10	197,720
Euro	113,100	63,152	6,969	6,800	-	190,021
Other	38,781	19,068	34,844	-	-	92,693
Total	314,002	96,490	53,886	16,046	10	480,434

2. **Excessive risk concentration**

Excessive concentration arises when a number of counterparties are engaged in similar business activities, in the same geographical region, or have certain economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Risk concentration indicates the relative sensitivity of the Bank's performance to developments affecting a particular industry.

In order to avoid excessive risk concentration, the Bank's policies and procedures include specific guidelines to maintain a diversified investment portfolio.



The excessive geographic risk concentration underlying the Bank's financial assets and liabilities is as follows:

	December 31, 2021				
	NIS million				
	Israel	Europe	USA	ROW	Total
Assets					
Assets abroad					
Cash and cash equivalents	-	158,000	10,207	2,663	170,870
Foreign currency bonds	-	93,724	188,920	91,221	373,865
Shares	-	19,027	75,610	20,838	115,475
Derivative financial instruments	-	(65,625)	157,622	(89,332)	2,665
Other foreign currency assets	-	3,490	286	3	3,779
The IMF	-	-	-	14,534	14,534
BIS investment	-	-	-	398	398
Local assets					
Local currency bonds	86,654	-	-	-	86,654
Loans to financial institutions	40,128	-	-	-	40,128
Other local currency assets	200	-	-	-	200
Total assets	126,982	208,616	432,645	40,325	808,568
Liabilities					
Liabilities abroad					
Derivative financial instruments	-	(8,496)	20,405	(11,564)	345
Other foreign currency liabilities	-	17,992	441	2	18,435
The IMF	-	-	-	12,013	12,013
Local liabilities					
Banknotes and coins in circulation	113,078	-	-	-	113,078
Reserves of banking corporations against reserve requirement	81,468	-	-	-	81,468
Time deposits	474,005	-	-	-	474,005
Short-term bills (<i>makam</i>)	114,984	-	-	-	114,984
Government reserves	49,722	-	-	-	49,722
Other local currency liabilities	8,816	-	-	-	8,816
Total liabilities	842,073	9,496	20,846	451	872,866



	December 31, 2020				
	NIS million				
	Israel	Europe	USA	ROW	Total
Assets					
Assets abroad					
Cash and cash equivalents	-	102,739	2,580	27,416	132,735
Foreign currency bonds	-	122,448	157,287	67,964	347,699
Shares	-	19,390	38,203	15,633	73,226
Derivative financial instruments	-	7,311	(16,938)	10,093	466
Other foreign currency assets	-	10,871	1,507	5	12,383
The IMF	-	-	-	6,606	6,606
BIS investment	-	-	-	399	399
Local assets					
Local currency bonds	50,345	-	-	-	50,345
Loans to financial institutions	21,061	-	-	-	21,061
Other local currency assets	188	-	-	-	188
Total assets	71,594	262,759	182,639	128,116	645,108
Liabilities					
Liabilities abroad					
Derivative financial instruments	-	63,411	(146,916)	87,547	4,042
Other foreign currency liabilities	-	11,907	-	-	11,907
The IMF	-	-	-	4,100	4,100
Local liabilities					
Banknotes and coins in circulation	105,805	-	-	-	105,805
Reserves of banking corporations against reserve requirement	55,017	-	-	-	55,017
Time deposits	365,002	-	-	-	365,002
Short-term bills (<i>makam</i>)	86,975	-	-	-	86,975
Government reserves	47,625	-	-	-	47,625
Other local currency liabilities	8,408	-	-	-	8,408
Total liabilities	668,832	75,318	(146,916)	91,647	688,881

3. **Market risk**

Market risk is the risk that the value of a financial instrument will fluctuate because of changes in market terms such as interest rates, prices and exchange rates. Market risk comprises currency risk, interest risk and other price risks. Market risk arises from investments in financial instruments of interest, currencies and capital which are exposed to general and specific market fluctuations and to changes in market price volatility levels.

The risk measure CVaRp (Conditional Value at Risk) is used to quantify the market risk (price risk and currency risk). It measures the risk in terms of the expected loss on the investment portfolio in a specific time period, for a given probability (p). It should be noted that CVaRp is a forward-looking (ex-ante) indicator, affected by changes in the portfolio holdings and the volatility of the portfolio assets, but is based on the past levels of volatility. In the guidelines, the Monetary Committee set the maximum level of risk for the reserves, so that given the worst 5 percent of possible outcomes, the average loss—the CVaR5%—would not be greater than 900 basis points over a one-year horizon. This risk profile became effective in April 2021 when the new guidelines came into force (before the change, the CVaR5% was 475 basis points over a one-year horizon). This risk level was set with the goal of limiting the short-term risk and increasing the probability of maintaining the purchasing power of the reserves in the intermediate term. The Monetary Committee regularly evaluates the conditions under which the level of risk was set, and may change this level if material changes in these conditions occur. At the beginning of 2021, the Monetary Committee set the CVaR5% at about 600 basis points (in 2020 – 320 basis points).

- a. **Foreign exchange rate risk** – the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates against the shekel. The Bank's asset value is exposed to exchange rate fluctuations in the main foreign currencies against the shekel given the currency composition of the Bank's assets.

The overall exposure can be mitigated to reduce the foreign exchange rate risk by diversifying the currency basket.

The Bank's main exposure to foreign exchange rate risk arises from the investments in foreign exchange reserves. At the end of 2021, the target currency composition of foreign exchange reserves is 67.4 percent in USD, 29.9 percent in Euro and 2.7 percent in Pound Sterling (in 2020 - 67.4 percent in USD, 30.1 percent in Euro and 2.5 percent in Pound Sterling).

Based on the guidelines of the Bank's investment policy, a maximum 10 percent deviation from the target currency composition is allowed based on the strategic allocation for that year and another deviation of up to 2 percent of the allocation in the short and medium range.



The Bank's overall currency exposure:

	December 31, 2021				
	NIS million				
	USD	Euro	NIS	Other	Total
Assets					
Assets abroad					
Cash and cash equivalents	10,207	152,738	-	7,925	170,870
Foreign currency bonds	217,643	70,317	-	85,905	373,865
Shares	78,576	12,812	-	24,087	115,475
Derivative financial instruments	108,523	(34,152)	-	(71,706)	2,665
Other foreign currency assets	287	1,274	-	2,218	3,779
The IMF	-	-	-	14,534	14,534
BIS investment	-	-	-	398	398
Local assets					
Local currency bonds	-	-	86,654	-	86,654
Loans to financial institutions	-	-	40,128	-	40,128
Other local currency assets	103	-	97	-	200
Total assets	415,339	202,989	126,879	63,361	808,568
Liabilities					
Liabilities abroad					
Derivative financial instruments	(15,787)	9,382	-	6,750	345
Other foreign currency liabilities	8,250	10,183	-	2	18,435
The IMF	-	-	-	12,013	12,013
Local liabilities					
Banknotes and coins in circulation	-	-	113,078	-	113,078
Reserves of banking corporations against reserve requirement	7,886	-	73,582	-	81,468
Time deposits	-	-	474,005	-	474,005
Short-term bills (<i>makam</i>)	-	-	114,984	-	114,984
Government reserves	5,407	262	44,053	-	49,722
Other local currency liabilities	-	-	8,816	-	8,816
Total liabilities	5,756	19,827	828,518	18,765	872,866
Total net balance sheet currency	409,583	183,162	(701,639)	44,596	(64,298)
Off-balance sheet balances					
Futures	(44)	47	-	-	3
Total currency exposure	409,539	183,209	(701,639)	44,596	(64,295)
Effect on profit or loss:					
1% exchange rate increase	12,737	6,449			
1% exchange rate decrease	(12,737)	(6,449)			



	December 31, 2020				
	NIS million				
	USD	Euro	NIS	Other	Total
Assets					
Assets abroad					
Cash and cash equivalents	8,511	87,241	-	36,983	132,735
Foreign currency bonds	197,000	92,584	-	58,115	347,699
Shares	39,786	15,765	-	17,675	73,226
Derivative financial instruments	(7,143)	976	-	6,633	466
Other foreign currency assets	9,551	1,886	-	946	12,383
The IMF	-	-	-	6,606	6,606
BIS investment	-	-	-	399	399
Local assets					
Local currency bonds	-	-	50,345	-	50,345
Loans to financial institutions	-	-	21,061	-	21,061
Other local currency assets	106	-	82	-	188
Total assets	247,811	198,452	71,488	127,357	645,108
Liabilities					
Liabilities abroad					
Derivative financial instruments	(130,561)	42,206	-	92,397	4,042
Other foreign currency liabilities	11,811	96	-	-	11,907
The IMF	-	-	-	4,100	4,100
Local liabilities					
Banknotes and coins in circulation	-	-	105,805	-	105,805
Reserves of banking corporations against reserve requirement	1,518	-	53,499	-	55,017
Time deposits	-	-	365,002	-	365,002
Short-term bills (<i>makam</i>)	-	-	86,975	-	86,975
Government reserves	5,777	392	41,456	-	47,625
Other local currency liabilities	-	-	8,408	-	8,408
Total liabilities	(111,455)	42,694	661,145	96,497	688,881
Total net balance sheet currency	359,266	155,758	(589,657)	30,860	(43,773)
Off-balance sheet balances					
Futures	245	(4)	-	-	241
Total currency exposure	359,511	155,754	(589,657)	30,860	(43,532)
Effect on profit or loss:					
1% exchange rate increase	11,558	6,143			
1% exchange rate decrease	(11,558)	(6,143)			



- b. **Interest rate risk** – the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

The Bank's exposure to fair value interest rate risk mainly arises from its investments in foreign exchange reserves. A significant portion of the foreign exchange reserves are invested in government bonds. The value of fixed interest instruments is affected by changes in interest rates in these countries which affect prices. Based on the investment policy, every currency portfolio is allocated a portfolio duration.

The portfolio duration measures the sensitivity of the investments to changes in interest rates. At the end of 2021, the adjusted duration of the foreign exchange reserves was similar to 2020 at 2.0 years. This means that a 1 percent decrease in the interest rate translates into a 2 percent increase in bond prices. The interest rate risk is monitored by a daily measurement of the portfolio's duration.

Analysis of the sensitivity of the Bank's profits to changes in interest rate on the foreign exchange reserve portfolio:

	In currency benchmark terms ⁶ and in basis points			
	2021		2020	
	100bp	50bp	100bp	50bp
Increase	(165)	(84)	(171)	(87)
Decrease	116	61	53	42

In the local market activities, this risk mainly arises from changes in the value of collaterals received in liquidity transactions. The collaterals expose the Bank to the risk of reduced or lost value due to the use of margins and haircuts that reduce value and enable the effective loan amount to drop below the collaterals received.

4. **Liquidity risk**

Liquidity risk is the risk arising from the inability to sell a financial instrument when needed or from a loss incurred in a sale due to the absence of market depth as well as the risk that the Bank will encounter difficulties in meeting cash-settled or other financial asset settled financial liabilities.

To allow immediate response to financial challenges arising in an emergency or crisis, a suitable portion of the foreign exchange reserves must be invested in assets that are readily available in large amounts with short notice and without impairment to the realization value.

⁶ The currency benchmark is the currency basket used for measuring the returns on the foreign exchange reserves. See more information in the annual review of the management of foreign exchange reserves.

The assets in which the reserves are invested are classified according to liquidity levels, from highly liquid assets that are readily realizable within less than a month to low liquidity assets whose realization period exceeds three months. The market division sets a minimum investment grade for high liquidity assets and a maximum investment grade for low liquidity assets.

The classification of the reserves into the various liquidity levels is assessed by the market division on an ongoing basis and reported on a quarterly basis to the Monetary Committee.

The table below summarizes the maturity profile of the financial assets and liabilities included in the Bank's foreign exchange reserves based on contractual undiscounted payments. The asset liquidity level does not necessarily depend on the asset maturity date.

	December 31, 2021					
	NIS million					
	On call to 3 months	4 months to a year	1 to 5 years	Over 5 years	No maturity date	Carrying amount
Assets abroad						
Cash and cash equivalents	170,870	-	-	-	-	170,870
Foreign currency securities	69,388	59,465	178,473	66,539	115,475	489,340
Derivative financial instruments	1,912	753	-	-	-	2,665
Other foreign currency assets	-	1,642	1,598	-	539	3,779
The IMF	-	-	-	35	14,499	14,534
Liabilities abroad						
Derivative financial instruments	248	97	-	-	-	345
Other foreign currency liabilities	16,757	-	-	-	1,678	18,435
Total foreign exchange reserves	225,165	61,763	180,071	66,574	128,835	662,408



December 31, 2020						
NIS million						
	On call to 3 months	4 months to a year	1 to 5 years	Over 5 years	No maturity date	Carrying amount
Assets abroad						
Cash and cash equivalents	132,735	-	-	-	-	132,735
Foreign currency securities	64,531	55,303	165,982	61,883	73,226	420,925
Derivative financial instruments	351	115	-	-	-	466
Other foreign currency assets	-	8,966	-	-	3,417	12,383
The IMF	-	-	-	76	6,530	6,606
Liabilities abroad						
Derivative financial instruments	3043	999	-	-	-	4,042
Other foreign currency liabilities	11,811	-	-	-	96	11,907
Total foreign exchange reserves	182,763	63,385	165,982	61,959	83,077	557,166

5. **Operational risk**

The Bank is exposed to operational risks. Operational risk is the risk of loss resulting from ineffective or failed internal processes, people, systems, or external events that can disrupt the flow of business operations. The Bank is exposed to the following subcategories of operational risks: legal, IT, HR, physical security, cybersecurity, projects, third parties, business continuity and regulation. Operational risks can lead to a financial loss, damage to reputation or failure in achieving the Bank's business targets. In response, the Bank has developed a central risk management system that identifies and mitigates the operational risks and enhances its internal control system.

NOTE 12 | FAIR VALUE OF FINANCIAL ASSETS AND LIABILITIES

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date whether or not the price can be directly measured or evaluated using a valuation technique.

Fair value measurement is based on the assumption that the transaction will take place in the asset's or the liability's principal market, or in the absence of a principal market, in the most advantageous market.

The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.



Fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The Bank uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximizing the use of relevant observable inputs and minimizing the use of unobservable inputs.

All assets and liabilities measured at fair value or for which fair value is disclosed are categorized into levels within the fair value hierarchy based on the lowest level input that is significant to the entire fair value measurement:

Level 1 - quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2 - inputs other than quoted prices included within Level 1 that are observable directly or indirectly.

Level 3 - inputs that are not based on observable market data (valuation techniques which use inputs that are not based on observable market data).

The investment instruments held by the Bank are mostly ranked as Level 1 (quoted market prices) in the fair value hierarchy.

The fair value of the financial assets and liabilities shown in the Statement of Financial Position:

	Fair value at December 31,		Fair value hierarchy	Parameters used to measure fair value
	2021	2020		
	NIS million			
Financial assets / liabilities at fair value through profit or loss:				
Government, multinational and public sector bonds	302,348	276,001	Level 1	Quoted price in active market
Corporate bonds	38,324	31,458	Level 1	Quoted price in active market
Commercial securities	23,927	30,515	Level 2	Interest curve
Mortgage backed securities	9,266	9,725	Level 1	Quoted price in active market
Shares	115,475	73,226	Level 1	Quoted price in active market
Derivative financial instruments - assets	2,665	466	Level 2	Interest curve
Derivative financial instruments – liabilities	(345)	(4,042)	Level 2	Interest curve
Total financial assets / liabilities at fair value through profit or loss	491,660	337,974		
Financial assets at fair value through other comprehensive income:				
BIS investment	398	399	Level 3	Fair value adjustments to net book value



The fair value and carrying amount of the financial assets and liabilities shown in the Statement of Financial Position:

	December 31, 2021			December 31, 2020			Fair value hierarchy
	Fair value	Carrying amount	Difference	Fair value	Carrying amount	Difference	
	NIS million						
Financial assets at amortized cost:							
Short-term deposits*	3,240	3,240	-	8,966	8,966	-	Level 2
Other foreign currency assets*	539	539	-	3,417	3,417	-	Level 2
The IMF*	14,534	14,534	-	6,606	6,606	-	Level 2
Local currency bonds	88,476	86,654	1,822	52,889	50,345	2,544	Level 1
Loans to financial institutions*	40,128	40,128	-	21,061	21,061	-	Level 2
Other local assets*	200	200	-		-		Level 2
Financial liabilities at amortized cost:							
Securities purchased in repo agreements*	(16,754)	(16,754)	-	(11,811)	(11,811)	-	Level 2
Other liabilities abroad	(1,681)	(1,681)	-	(4,042)	(4,042)	-	Level 2
The IMF*	(12,013)	(12,013)	-	(4,100)	(4,100)	-	Level 2
Banknotes and coins in circulation*	(113,078)	(113,078)	-	(105,805)	(105,805)	-	Level 2
Reserves of banking corporations against reserve requirement*	(81,468)	(81,468)	-	(55,017)	(55,017)	-	Level 2
Time deposits*	(474,005)	(474,005)	-	(365,002)	(365,002)	-	Level 2
Short-term bills (makam)	(114,991)	(114,984)	(7)	(86,980)	(86,975)	(5)	Level 1
Government reserves*	(49,722)	(49,722)	-	(47,625)	(47,625)	-	Level 2
Other local liabilities*	(8,816)	(8,816)	-	(8,408)	(8,408)	-	Level 2

* The carrying amount approximates the fair value.

NOTE 13 | SPECIAL COMMITMENTS AND CONTINGENT LIABILITIES

Accounting policies

a. Provisions

A provision is recognized when the Bank has a present legal or constructive obligation as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. The amount recognized as a provision is measured as the best estimate of the expense needed to settle the present obligation at the end of the reporting period. When the effect of the time value of money is material, the provision amount is the present value of the expected expense that will be incurred to settle the obligation.

b. Contingent liabilities

Contingent liabilities are potential commitments that might arise from uncertain future events which are not controlled by the Bank and present obligations which have not been recognized since they cannot be measured reliably or whose payment is unlikely. Contingent liabilities are not recognized in the financial statements but are disclosed if they are material.

c. Contractual obligations

A contractual obligation is an enforceable legally binding agreement to make future payment for the purchase of goods or services. The amount of the contractual obligation is not recognized in the financial statements since the goods or services have yet to be provided to the Bank by the supplier or service provider.

**a. Special commitments – derivative financial instruments**

	December 31,	
	2021	2020
	NIS million	
Foreign exchange transactions		
Future receipt of foreign currency (currency swaps, forwards, spot)	165,451	151,466
Future delivery of foreign currency (currency swaps, forwards, spot)	163,133	155,170
Shekel-dollar exchange transactions		
Future receipt of dollars (forwards, spot)	796	1,471
Future delivery of shekels (forwards, spot)	795	1,470
Stock indices futures at fair value		
Obligation to buy	39	228
Interest futures at fair value		
Obligation to buy	(40)	-
Obligation to sell	(37)	-
Bond futures at fair value		
Obligation to buy	24	17
Obligation to sell	16	(4)

b. Contingent liabilities

1. When investing in BIS, the Bank of Israel is required to assume additional undertakings toward the institution beyond the actual callable capital, which may be exercised by the institution only in times of need, a scenario which is relatively unlikely. The balance of the above undertakings as of December 31, 2021 is NIS 53 million (December 31, 2020 - NIS 56 million).
2. There are several claims pending against the Bank of Israel. However, no provision has been recorded in the Bank's books in respect of these claims as it is the Bank's opinion, based on the opinion of its Legal Department, that the probability of these claims being upheld is low, or that the sums involved are not significant.



3. Renewal of the Bank's lease agreement - the Bank's lease from the ILA expired in late June 2016. Since then, the ILA has not renewed the lease agreement with the Bank and has not notified the Bank of any costs that are expected to be incurred as a result of the renewal despite the Bank's recurring applications to the ILA and joint meetings held to promote the issue. The Bank is unable to assess when the ILA will renew the lease agreement and whether the renewal will consist of any payment or charge and if so, how much such charge will be and how it will apply - from the date of expiration of the old lease agreement or from the date of renewal only. Therefore, no provision was recorded in the Bank's books.

NOTE 14 | INTEREST INCOME FROM FOREIGN EXCHANGE RESERVES, NET

	Year ended December 31,	
	2021	2020
	NIS million	
Demand deposits	(249)	(119)
Short-term deposits	(16)	33
Tradable securities	2,769	3,451
Securities purchased under r. repo agreements or sold under repo agreements	12	10
The IMF	16	14
Total	2,532	3,389

NOTE 16 | GAIN OR LOSS FROM FAIR VALUE REVALUATION OF FINANCIAL ASSETS FROM ACTIVITIES ABROAD

This line item consists of both realized and unrealized gains (losses).

Realized gains (losses) derive from sold or derecognized financial instruments.

Unrealized gains (losses) derive from financial instruments which the Bank keeps holding as part of its investments.



Following are the realized and unrealized gains (losses) according to type of financial instrument:

	Year ended December 31,	
	2021	2020
	NIS million	
From bonds ¹		
Realized	(171)	1,609
Unrealized	(6,434)	3,477
	(6,605)	5,086
From shares ²		
Realized	3,797	6,083
Unrealized	15,740	3,498
	19,537	9,581
From derivative financial instruments ³		
Realized	864	2,602
Unrealized	(234)	142
	630	2,744
Total	13,562	17,411

¹ Bonds

Realized – post-sale accumulated gain or loss.

Unrealized – revalued to fair value of financial assets measured at fair value through profit or loss.

² Shares

Realized – post-sale accumulated gain or loss including dividend income.

Unrealized – revalued to fair value of financial assets measured at fair value through profit or loss.

³ Derivative financial instruments

Realized – post-sale accumulated income or expenses from realization of derivative financial instruments and revalued to fair value up to the amount of accrued interest inherent to the transaction.

Unrealized – revalued to fair value of financial assets measured at fair value through profit or loss.



NOTE 16 | MISCELLANEOUS EXPENSES FROM ACTIVITIES ABROAD, NET

	Year ended December 31,	
	2021	2020
	NIS million	
Tax expenses on investments abroad	62	46
Foreign currency commissions ¹	76	53
Total	138	99

¹ This line item mainly includes expenses from commissions on the Bank of Israel's financial activity.

NOTE 17 | INTEREST FROM LOCAL FINANCIAL INSTRUMENTS

Following are details of interest income and expense from the Bank's local activity:

	Year ended December 31,	
	2021	2020
	NIS million	
Interest income:		
From local currency government bonds ¹	864	187
From corporate bonds ²	90	15
From loans to financial institutions ¹	23	8
Other interest income ²	77	76
	1,054	286
Interest expenses:		
On short-term bills (<i>makam</i>) ¹	(40)	(183)
On time deposits ¹	(413)	(351)
On government local currency balances ¹	(380)	(334)
On government foreign currency balances ¹	(2)	(4)
Other interest expenses ²	(76)	(74)
	(911)	(946)
Total net interest income (expense) from local financial instruments	143	(660)

¹ See Note 5.

² See Note 6.



NOTE 18 | GAIN FROM FAIR VALUE REVALUATION OF FINANCIAL ASSETS FROM LOCAL ACTIVITIES

This line item mainly consists of gains from shekel-dollar swaps in the local market entered into by the Bank in 2020 in the context of the market intervention measures adopted due to the Covid-19 crisis to supply dollars to the local banks.

NOTE 19 | MISCELLANEOUS INCOME FROM LOCAL ACTIVITIES, NET

This line item mainly consists of income from commissions deriving from the Bank's financial activity in the local market.

NOTE 20 | EXCHANGE RATE DIFFERENTIALS

Exchange rate differentials are classified as realized when the foreign currency reserve is partially or fully written down. The amount recognized as realized is calculated at the exchange rate underlying the sale of the reserves as opposed to the weighted average cost of purchasing the foreign currency.

The calculation of realized gains is done separately for each currency without inter-offsetting of other foreign exchange reserves.

Following is a breakdown of the Bank's income and expenses from realized and unrealized exchange rate differentials based on the different items:

	Year ended December 31,	
	2021	2020
	NIS million	
Assets:		
Foreign exchange reserves	(36,307)	(25,186)
Liabilities:		
Government reserves	378	518
Reserves of banking corporations	35	690
IMF reserves	523	131
Other	1	-
Total	(35,370)	(23,847)
Realized exchange rate differentials	268	410
Unrealized exchange rate differentials	(35,638)	(24,257)

This line item mainly consists of exchange rate differentials on reserves in euro and dollar due to the strengthening of the shekel against these currencies in the year. In 2020, the amount mainly derived from the dollar due to the strengthening of the shekel against the dollar.



NOTE 21 | GENERAL AND ADMINISTRATIVE EXPENSES

	Year ended December 31,	
	2021	2020
	NIS million	
Employee salaries and rights	427	395
Pension and benefits to employees and pensioners ¹	179	183
Depreciation and amortization	105	103
General expenses	151	*) 156
Total	862	*) 837

*) An amount of about NIS 2 million was reclassified to the line item "expenses of printing banknotes and minting coins".

¹ Expenses in respect of actuarial obligation for post-employment benefits to employees and pensioners.

NOTE 22 | OTHER INCOME, NET

	Year ended December 31,	
	2021	2020
	NIS million	
Income from fees ¹	31	29
Miscellaneous expenses	-	2
Total	31	27

¹ This item includes mainly income from fees from the Credit Data System and the Real Time Gross Settlement System.

NOTE 23 | TRANSITION TO IFRS

As described in Note 2a above, these financial statements are the Bank's first annual financial statements prepared in conformity with IFRS. The Bank first adopted IFRS in 2021 and therefore the date of transition to IFRS reporting is January 1, 2020. The Bank prepared an opening balance sheet as of the date of transition to IFRS reporting.

Prior to adopting IFRS, the Bank prepared its financial statements in conformity with Israeli GAAP, as adjusted for the special activities of a central bank and as practiced by other central banks. The Bank's last annual financial statements prepared in conformity with Israeli GAAP are as of December 31, 2020 and for the year then ended. The Bank's first annual financial statements prepared in conformity with IFRS are as of December 31, 2021 and for the year then ended.

Accordingly, the Bank discloses the following reconciliations from reporting in conformity with Israeli GAAP to reporting in conformity with IFRS as of January 1, 2020 (the date of transition to IFRS reporting), as of December 31, 2020 and for the year ended December 31, 2020.

According to IFRS 1, "First-time Adoption of International Financial Reporting Standards", the application of IFRS to the opening balance as of the date of transition to IFRS reporting must be done retrospectively.



Reconciliations to the Statement of Financial Position (based on the new reporting framework excluding revaluation accounts):

	December 31, 2020			January 1, 2020		
	NIS million			NIS million		
	Israeli GAAP	IFRS reconciliations	IFRS	Israeli GAAP	IFRS reconciliations	IFRS
ASSETS						
Assets abroad						
Foreign exchange reserves:						
Cash and cash equivalents	126,785	5,950	132,735	96,596	11,332	107,928
Foreign currency securities	420,925	-	420,925	318,589	-	318,589
Derivative financial instruments	469	(3)	466	760	18	778
Other assets	18,333	(5,950)	12,383	15,130	(11,332)	3,798
The IMF	6,606	-	6,606	6,084	-	6,084
BIS investment	282	117	399	282	102	384
Total assets abroad	573,400	114	573,514	437,441	120	437,561
Local assets						
Local currency bonds	50,345	(4)	50,341	1,677	-	1,677
Loans to financial institutions	21,061	-	21,061	-	-	-
Other assets	188	-	188	199	-	199
Fixed assets and Intangible assets	823	-	823	833	-	833
Total local assets	72,417	(4)	72,413	2,709	-	2,709
Total assets	645,817	110	645,927	440,150	120	440,270



	December 31, 2020			January 1, 2020		
	NIS million			NIS million		
	Israeli GAAP	IFRS reconciliations	IFRS	Israeli GAAP	IFRS reconciliations	IFRS
LIABILITIES						
Liabilities abroad						
Foreign exchange reserves:						
Derivative financial instruments	4,062	(20)	4,042	1,075	3	1,078
Other liabilities	11,907	-	11,907	579		579
The IMF	4,100	-	4,100	4,236		4,236
Total liabilities abroad	20,069	(20)	20,049	5,890	3	5,893
Local liabilities						
Banknotes and coins in circulation	105,805	-	105,805	87,178		87,178
Reserves of banking corporations against reserve requirement	55,017	-	55,017	45,687		45,687
Time deposits	365,002	-	365,002	194,011		194,011
Short-term bills (<i>Makam</i>)	86,975	-	86,975	119,870		119,870
Government reserves	47,625	-	47,625	18,184		18,184
Other liabilities	8,408	-	8,408	7,791		7,791
Total local liabilities	668,832	-	668,832	472,721	-	472,721
Total liabilities	688,901	(20)	688,881	478,611	3	478,614
Revaluation accounts	27,197	(27,197)	-	17,648	(17,648)	-
Bank's equity (deficit equity) and reserves						
Bank's equity (deficit equity)						
Bank's equity and general reserve	3,985	-	3,985	3,985	-	3,985
Accumulated deficit	(74,262)	-	(74,262)	(60,094)	-	(60,094)
Revaluation reserves	-	27,327	27,327	-	17,765	17,765
Total Bank's equity (deficit equity) and reserves	(70,277)	27,327	(42,950)	(56,109)	17,765	(38,344)
Total liabilities and equity	645,821	110	645,931	440,150	120	440,270

**Reconciliations to the Statement of Financial Position as of January 1, 2020 and December 31, 2020:**

Upon the transition to IFRS reporting, the following reconciliations have been made which affect the balances in the Statement of Financial Position:

- Cash and cash equivalents and other assets – reclassification of short-term deposits whose original maturity does not exceed three months from the investment date from other foreign currency assets to cash and cash equivalents.
- Fair value measurement of derivative financial instruments.
- Remeasurement of BIS investment from amortized cost to fair value.
- Recording an allowance for ECLs in respect of local currency corporate bonds.
- Inclusion of unrealized gains from revaluation accounts in equity under revaluation reserves.

Changes to the structure of the Statement of Financial Position from 2021:

The change mainly arises from the change in presentation of assets and liabilities based on location: local or abroad. Prior to the change, the assets and liabilities were presented based on currency: local or foreign.

Reconciliations to the Statement of Profit or Loss and Other Comprehensive Income:

	Year ended December 31, 2020
	NIS million
Loss as per Israeli GAAP	(14,168)
Changes in measurement for reconciliation to IFRS:	
Effect on profit or loss:	
Exchange rate differentials	2,337
Revaluation of financial assets measured at fair value through profit or loss	7,402
Other	(71)
Total effect of transition to IFRS on profit or loss	9,668
Effect on other comprehensive income (loss):	
Remeasurement of defined benefit plan	(121)
Investments in equity instruments measured at fair value through other comprehensive income	15
Total effect of transition to IFRS on other comprehensive income (loss)	(106)
Comprehensive loss as per IFRS	(4,606)

Reconciliations to the Statement of Profit or Loss and Other Comprehensive Income for the year ended December 31, 2020:

Upon the transition to IFRS reporting, the following gains and losses which affect the income in the year ended December 31, 2020 have been reconciled in the Statement of Profit or Loss and Other Comprehensive Income:

- The inclusion of unrealized gains from exchange rate differentials on foreign currency balances in profit or loss reduced the loss as per IFRS by about NIS 2,337 million.
- The inclusion of unrealized gains from fair value revaluation of financial instruments in profit or loss reduced the loss as per IFRS by about NIS 7,402 million, of which about NIS 3,677 million is in fair value revaluation of bonds, about NIS 3,583 million in fair value revaluation of shares, and about NIS 142 million in fair value revaluation of derivative financial instruments (of which about NIS 2 million is from fair value remeasurement of derivative financial instruments previously excluded from unrealized gains).
- The inclusion of other unrealized losses increased the loss as per IFRS by about NIS 71 million, of which about NIS 53 million in foreign currency bond indexation differentials, about NIS 14 million in local currency bond indexation differentials and about NIS 4 million in expenses on ECLs in respect of local currency corporate bonds.

The following unrealized gains from the remeasurement of defined benefit plan and change in fair value of investments in equity instruments which affect the comprehensive income (loss) in the year ended December 31, 2020 have been reconciled in the Statement of Other Comprehensive Income (Loss):

- The inclusion of losses from remeasurement of defined benefit plan in other comprehensive income (loss) increased the comprehensive loss as per IFRS by about NIS 121 million.
- The inclusion of gains from change in fair value of the BIS investment in other comprehensive income (loss) reduced the comprehensive loss as per IFRS by about NIS 15 million.

Changes to the structure of the Statement of Profit or Loss and Other Comprehensive Income from 2021:

The change mainly arises from the change in presentation of the Bank's activities based on the location: local activities or activities abroad.



NOTE 24 | DISTRIBUTABLE PROFITS

The distribution of the Bank's profits is governed by the Bank of Israel Law. According to Section 76(a) of this law, the Bank's net income will not include unrealized gains as per the annual financial statements. Distributable profits are determined based on the income or loss as per IFRS (before other comprehensive income) with the following adjustments:

- Unrealized gains from exchange rate differentials on foreign currency balances accumulated in the reporting year are excluded from distributable profits;
- Unrealized gains from fair value revaluation accumulated in the reporting year are excluded from distributable profits;
- Unrealized gains from exchange rate differentials on foreign currency balances reported in previous periods and realized in the reporting year are included in distributable profits;
- Unrealized gains from fair value revaluation reported in previous periods and realized in the reporting year are included in distributable profits;
- Unrealized revaluation losses at year end are offset against credit balances in the proper revaluation reserve at the item level (currency or security) up to the amount of the credit balance. Balances that are not offset are excluded from distributable profits.

As per Section 76 of the Bank of Israel Law, within three months from each fiscal year end, the Bank will distribute to the Government its actual profits in keeping with the following guidelines:

1. If the Bank's capital is 2.5 percent or more of total assets, an amount equivalent to the net profits less the surplus balance if it is negative, shall be transferred to the Government.
2. If the Bank's capital exceeds 1 percent of total assets but is less than 2.5 percent of total assets, an amount equal to 50 percent of net profits less the surplus balance if it is negative shall be transferred to the Government.
3. If the Bank's capital is 1 percent or less of total assets, profits shall not be transferred to the Government.

The Bank may record capital funds arising from the application of IFRS provided that the balance of net income that has not been distributed to the Government will be included in retained earnings and not recognized as a separate capital item, unless otherwise agreed between the Governor and the Minister of Finance.



The calculation of the loss carried to accumulated deficit as per the Bank of Israel Law is as follows:

	Year ended December 31,	
	2021	2020
	NIS million	
Loss in the year	(20,133)	(4,500)
Less:		
Amounts reclassified to revaluation reserve of unrealized exchange rate differentials	(2,098)	2,747
Amounts reclassified to revaluation reserve of unrealized gains from fair value adjustments	12,933	13,616
Other accounting adjustments	497	(40)
	11,332	16,323
Add:		
Amounts reclassified from revaluation reserve of unrealized exchange rate differentials	268	410
Amounts reclassified from revaluation reserve of unrealized gains from fair value adjustments	1,686	6,214
Other accounting adjustments	111	31
	2,065	6,655
Total loss recognized in the year	(29,400)	(14,168)

NOTE 25 | EVENTS AFTER THE REPORTING DATE

In early 2022, a new risk factor came into play in global activity arising from the war between Russia and Ukraine. As of the date of approval of the financial statements, there has been a decline in share indices invested by the Bank of Israel. At present, the effect of the war on the financial statements for 2022 cannot be assessed.