

**Rating Action: Moody's upgrades Israel Discount Bank's deposit ratings to A2, outlook changed to stable**

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15 Jun 2021

Limassol, June 15, 2021 -- Moody's Investors Service (Moody's) has today upgraded Israel Discount Bank Ltd. (IDB)'s long-term bank deposit ratings to A2 from A3 and changed the outlook on these to stable from positive. Concurrently, the rating agency also upgraded the bank's short-term bank deposit ratings to Prime-1 from Prime-2, its long-term Counterparty Risk Ratings (CRR) to A1 from A2, its long-term Counterparty Risk (CR) Assessment to A1(cr) from A2(cr), and its standalone Baseline Credit Assessment (BCA) and Adjusted BCA to baa2 from baa3. The short-term CRR and CRA were affirmed at Prime-1 and Prime-1(cr) respectively.

The ratings upgrade reflects IDB's recent improvements in its profitability, strengthening resiliency in times of stress, given continued focus on efficiencies and robust growth potential. The ratings upgrade also considered ongoing improvement in the bank's asset risk profile because of growth in lower-risk assets, such as residential mortgages in Israel. The stable outlook reflects the rating agency's expectation that IDB will be able to sustain the improvements in its solvency and that the bank's capital will remain broadly stable, while loan quality will deteriorate only moderately following last year's economic downturn buffered by a substantial stock of provisions.

A full list of affected ratings and assessments can be found at the end of this press release.

**RATINGS RATIONALE**

**-- RATINGS UPGRADE**

The upgrade of IDB's deposit ratings to A2 from A3 primarily reflects improvements in its solvency profile driven by improving profitability and gradually lower asset risk.

IDB's profitability will continue to benefit from ongoing cost initiatives and the bank's enhanced growth potential. Efficiency plans, which include more recently the bank's largest ever early retirement plan, have significantly lowered operating expenses in recent years. Operating costs, excluding one-offs, declined to 2.0% of assets in the first quarter of 2021, from 2.1% in 2020 and 2.5% in 2018. In combination with improvements on the revenue side, with the bank's pre-provision income growing on average by around 5% since 2018, the bank's cost-to-income ratio, adjusted for one-off items, improved to 60.6% in the first quarter of 2021, compared to 66.1% in 2018. Nevertheless, the bank's cost base remains higher than its domestic peers, and the bank continues to focus on improving it further. A lean operating cost base improves a financial institution's ability to absorb potential losses, strengthening resiliency in times of stress.

Following the pandemic-induced temporary decline in profitability in 2020, net income improved to 1.0% of tangible assets in the first quarter of 2021 from 0.5% in 2020 (excluding one-off items), although benefiting from provision reversals. IDB's profitability has consistently strengthened in the run-up to the pandemic-driven crisis, closing the gap with its domestic peers, with the bank's net income to tangible assets ratio averaging around 0.7% for the period 2017-2019 compared to an average of around 0.4% for the period 2014-2016.

The upgrade also reflects the ongoing reduction in asset risk for IDB's loan portfolio reflecting an increasing share of relatively lower-risk residential mortgages and more moderate overall loan growth going forward compared to the last few years, although still above the market average. Mortgages, a key strategic focus for the bank, grew by a high 15.7% year-over-year in the first quarter of 2021 and accounted for 22.4% of the bank's loan book compared to 19.6% as of the end of 2018. The bank's market share in this segment remained lower than its market share in other segments and affords significant potential for ongoing growth for IDB. Moody's considers housing loans in Israel as relatively lower risk because of the low level of household debt, macroprudential measures that enforce tight underwriting standards and the fundamentals of the housing market, with a structurally limited supply of new housing units providing price support. Lower borrower concentration levels in the bank's loan book also drive lower asset risk.

Moody's expects problems loans to increase moderately following the lifting of support measures to borrowers, but from a strong level and mitigated by the significant stock of collective provisions that the bank built in 2020,

with allowances on non-impaired loans accounting for 1.6% of gross non-impaired loans as of March 2021. IDB's relatively unseasoned portfolio, following rapid loan growth in recent years, was somewhat tested in the recent economic downturn. Problem loans to gross loans remained broadly stable at a relatively low level of 1.4% as of March 2021 (excluding a predominantly government-backed exposure that became more than 90 days overdue), compared to 1.3% and 1.2% as of the end of 2020 and 2019 respectively, reflecting measures by the Israeli authorities to support borrowers, as well as, loan payment deferrals extended by the bank that deferred the impact of the crisis on asset quality. However, Moody's notes that loans with payment deferrals declined sharply to just 1.4% of IDB's total loans as of March 2021, compared to the peak level of 8.4% as of June 2020, in line with the system.

The bank's ratings also reflect adequate but modest capital buffers, with a tangible common equity/ risk-weighted assets ratio of 9.5% as of March 2021. Although this level is below that of similarly-rated international peers, this reflects the regulator's conservative approach to risk-weighting, especially on mortgage lending, that results in higher loss-absorption buffers than capital ratios show.

IDB benefits from a favourable funding structure supported by a large and granular deposit base with a high proportion of retail deposits helped by Israel's strong savings culture. This comfortably funds the bank's loan portfolio, with a net loans-to-deposits ratio of 82% as of March 2021. IDB also maintains comfortable liquidity buffers at 31% of tangible banking assets as of March 2021.

IDB's A2 deposit ratings continue to incorporate three notches of government support uplift because of Moody's assessment of a very high probability of extraordinary support from the Government of Israel (A1 stable). This assessment is based on the bank's systemic importance as one of the country's five large banking groups and the Israeli government's long standing practice of injecting capital into systemically important banks in case of need.

#### -- STABLE OUTLOOK

The stable outlook reflects the rating agency's expectation that IDB will sustain the improvements in its profitability given continued focus on cost efficiencies and business growth potential because of Israel's robust economic growth potential, process improvements at the bank that reduce time to market and a number of digital initiatives that can capture a broader share of the population than the bank's current clientele. Moody's also expects that IDB will continue to grow the share of lower-risk mortgages in its portfolio, gradually moderating asset risk.

The stable outlook also reflects Moody's expectation that the bank's capital will remain broadly stable and that loan quality will deteriorate only moderately following last year's economic downturn buffered by a substantial stock of provisions.

#### FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

IDB's ratings could be upgraded following (1) materially strengthened capital buffers; and (2) a sustained improvement in the bank's recurring profitability beyond what is currently expected, without an increase in the credit risk profile.

Downward pressure could be exerted on IDB's ratings if deteriorating operating conditions lead to a material weakening in asset quality, or if the bank's capitalisation declines from current levels. If the bank does not sustain the ongoing improvements in its profitability and efficiency, or the reduction in asset risk, there could also be negative pressure on the ratings.

There could also be negative rating pressure if Moody's considers that the government's willingness or capacity to provide support has materially declined.

#### LIST OF AFFECTED RATINGS

..Issuer: Israel Discount Bank Ltd.

Upgrades:

....Adjusted Baseline Credit Assessment, Upgraded to baa2 from baa3

....Baseline Credit Assessment, Upgraded to baa2 from baa3

....Long-term Counterparty Risk Assessment, Upgraded to A1(cr) from A2(cr)

....Long-term Counterparty Risk Ratings, Upgraded to A1 from A2

....Short-term Bank Deposit Ratings, Upgraded to P-1 from P-2

....Long-term Bank Deposit Ratings, Upgraded to A2 from A3, Outlook Changed To Stable From Positive

Affirmations:

....Short-term Counterparty Risk Assessment, Affirmed P-1(cr)

....Short-term Counterparty Risk Ratings, Affirmed P-1

Outlook Action:

....Outlook, Changed To Stable From Positive

## PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Banks Methodology published in March 2021 and available at [https://www.moody's.com/researchdocumentcontentpage.aspx?docid=PBC\\_1261354](https://www.moody's.com/researchdocumentcontentpage.aspx?docid=PBC_1261354) . Alternatively, please see the Rating Methodologies page on [www.moody's.com](http://www.moody's.com) for a copy of this methodology.

## REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found at: [https://www.moody's.com/researchdocumentcontentpage.aspx?docid=PBC\\_79004](https://www.moody's.com/researchdocumentcontentpage.aspx?docid=PBC_79004).

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