

Various Rating Actions Taken On Israeli Banks On Sovereign Downgrade; All Outlooks Negative

October 9, 2024

Overview

- On Oct. 1, 2024, we lowered our sovereign ratings on Israel to 'A/A-1' from 'A+/A-1' on heightened geopolitical risk. The outlook on the long-term ratings is negative.
- In our view, this indicates a weaker likelihood of timely and sufficient extraordinary government support to Israeli banks.
- We are therefore lowering our long-term issuer credit ratings on Bank Hapoalim B.M., Bank Leumi le-Israel B.M., and Mizrahi Tefahot Bank Ltd.
- We also affirmed our ratings on Israel Discount Bank Ltd. (IDB) and its core subsidiary, Israel Discount Bank of New York (IDB NY).
- The outlooks on all these banks remain negative.

MILAN (S&P Global Ratings) Oct. 9, 2024--S&P Global Ratings today took rating actions on the following Israeli banks (for full details, please see the ratings list below):

- We lowered to 'BBB+' from 'A-' our long-term issuer credit ratings on Hapoalim, Leumi, and Mizrahi. At the same time, we affirmed our short-term issuer credit ratings on these banks at 'A-2'. The outlooks are negative.
- We affirmed our 'BBB+/A-2' long- and short-term issuer credit ratings on IDB and our 'BBB+' long-term issuer credit rating on its core subsidiary IDB NY. The outlook remains negative.

The rating actions follow the lowering of our sovereign ratings on Israel. We downgraded Israel because we see an increased likelihood that Israel's economy and public finances could be disrupted by its intensifying conflict with Hezbollah and the possible security threats should retaliatory rocket attacks be directed at Israel (see "Israel Long-Term Ratings Lowered To 'A' From 'A+' On Heightened Security Risk; Outlook Negative," published on Oct. 1, 2024). We now forecast growth of 2.2% in 2025, versus 5.0% previously. Assuming that the security situation stabilizes in the second half of 2025, we anticipate that a recovery would take hold from 2026. We also project that Israel's fiscal deficits for 2024 will widen to 9% of GDP, and will average about 5% over 2026-2027, as defense-related spending increases further.

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The deterioration of Israel's fiscal profile could indirectly affect the banking sector. A

lessening of the government's fiscal space would limit its ability to further support the economy in future. The government has already absorbed some of the economic shock related to the conflict and has been proactive in extending support to areas and sectors that have been affected, directly or indirectly. Ultimately, this has reduced the negative spillover effect on the banking system. The resilience of banks' performance over the past 12 months was also supported by the low unemployment rate (about 3.2% in April) and by the containing of the impact on real estate sector activity of the shortage of workers. As of the second half of 2024, the systemwide nonperforming loan (NPL) ratio was low at 1%, while resilient revenues enabled banks to build large provisions buffers. Return on equity averaged about 15% at the end of June 2024.

Our current base case already captures a significant deterioration in banks' operating environment.

We have already identified pockets of risk affecting tourism-focused businesses, small and midsize enterprises (SMEs), unsecured lending, and the real estate and construction segments, although we believe that the materialization of these risks could be delayed. In our base case, we assume an increase in credit losses, to 30-35 basis points, over 2024-2026, based on delayed asset quality issues, combined with the potential for reduced support from the government. Our assessment of the banking sector has not changed, but we continue to see high downside risk to banks' asset quality and profitability if the conflict further escalates.

That said, we consider that the sovereign rating action ultimately indicates a decrease in the government's capacity to offer timely and sufficient extraordinary support to Israeli banks.

We therefore removed the notch of uplift for government support that we previously incorporated in our long-term issuer credit ratings on Hapoalim, Leumi, and Mizrahi.

Bank Hapoalim B.M.

Pierre Hollegien

We downgraded Hapoalim because we no longer incorporate one notch of uplift for extraordinary government support in our rating. The bank's stand-alone credit profile (SACP), which remains at 'bbb+', is based on Hapoalim's relative strengths in the current difficult environment. These include its leading position in the Israeli market; its strong track record and conservative underwriting; and its robust capitalization, which is supported by resilient profitability. Our ratings on Hapoalim also incorporate its high concentration in the real estate sector.

We have affirmed our ratings on Hapoalim's subordinated contingent convertible bond because we do not expect the government to provide support for those instruments.

Outlook

The negative outlook on Hapoalim indicates our view that further escalation of the war could have negative implications for Hapoalim's creditworthiness over the next 12-24 months.

Downside scenario: We could lower the rating on Hapoalim if we downgraded Israel and considered that economic risks for banks in Israel had structurally increased to such an extent that it would undermine Hapoalim's asset quality, capitalization, or earnings.

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Upside scenario: We could revise the outlook to stable if we thought that security risks and the pressure on domestic economic prospects had lessened.

Hybrids: We do not assign outlooks to bank issue ratings. However, we will continue to notch down the ratings on Hapoalim's hybrids from the SACP. Therefore, we would lower our rating on the bank's rated subordinated instruments if we were to lower our SACP on Hapoalim.

Ratings score snapshot

	To	From
Issuer credit rating	BBB+/Negative/A-2	A-/Negative/A-2
Stand-alone credit profile	bbb+	bbb+
Anchor	bbb	bbb
Business position	Strong (+1)	Strong (+1)
Capital and earnings	Strong (+1)	Strong (+1)
Risk position	Moderate (-1)	Moderate (-1)
Funding and liquidity	Adequate (0)	Adequate (0)
Comparable ratings analysis	0	0
Support	0	+1
ALAC support	0	0
GRE support	0	0
Group support	0	0
Sovereign support	0	+1
Additional factors	0	0

ALAC--Additional loss-absorbing capacity. GRE--Government-related entity.

Bank Leumi le-Israel B.M.

Pierre Hollegien

We downgraded Leumi because we no longer incorporate one notch of uplift for extraordinary government support in our rating. The bank's SACP, which remains at 'bbb+', is based on Leumi's relative strengths in the current difficult environment. These include its earnings resiliency, strong franchise, and financial flexibility. Our ratings on Leumi also incorporate its high concentration in the real estate sector.

We have affirmed our ratings on Leumi's contingent convertible bond because we do not expect the government to provide support for those instruments.

Outlook

The negative outlook on Leumi indicates our view that further escalation of the war could have negative implications for Leumi's creditworthiness over the next 12-24 months.

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sector.

Downside scenario: We could lower the rating on Leumi if we downgraded Israel and considered that economic risks for banks in Israel had structurally increased to such an extent that it would undermine Leumi's asset quality, capitalization, or earnings.

Upside scenario: We could revise the outlook to stable if we thought that security risks and the pressure on domestic economic prospects had lessened.

Hybrids: We do not assign outlooks to bank issue ratings. However, we will continue to notch down the ratings on Leumi's hybrids from the SACP. Therefore, we would lower our rating on the bank's rated subordinated instruments if we were to lower our SACP on Leumi.

Ratings score snapshot

	To	From
Issuer credit rating	BBB+/Negative/A-2	A-/Negative/A-2
Stand-alone credit profile	bbb+	bbb+
Anchor	Bbb	bbb
Business position	Strong (+1)	Strong (+1)
Capital and earnings	Adequate (0)	Adequate (0)
Risk position	Moderate (-1)	Moderate (-1)
Funding and liquidity	Adequate (0)	Adequate (0)
Comparable ratings analysis	+1	+1
Support	0	+1
ALAC support	0	0
GRE support	0	0
Group support	0	0
Sovereign support	0	+1
Additional factors	0	0

ALAC--Additional loss-absorbing capacity. GRE--Government-related entity.

Mizrahi Tefahot Bank Ltd.

Regina Argenio

We downgraded Mizrahi because we no longer incorporate one notch of uplift for extraordinary government support in our rating. The bank's SACP, which remains at 'bbb+', is based on Mizrahi's relative strengths in the current difficult environment. These include its high earnings and capital buffers and resilient asset quality. Our ratings on Mizrahi also incorporate its high concentration in the local residential real estate sector and its recent expansion into SMEs and the construction segment, where it has a limited track record.

We have affirmed our ratings on Mizrahi's contingent convertible bond because we do not expect

the government to provide support for those instruments.

Outlook

The negative outlook on Mizrahi indicates our view that further escalation of the war could have negative implications for Mizrahi's creditworthiness over the next 12-24 months.

Downside scenario: We could lower the rating on Mizrahi if we downgraded Israel and considered that economic risks for banks in Israel had structurally increased to such an extent that it would undermine Mizrahi's asset quality, capitalization, or earnings. For example, significant asset quality and a deterioration in profitability could lead us to believe that the bank's risk-adjusted capital (RAC) ratio was unlikely to improve above 10% over the next 24 months.

Upside scenario: We could revise the outlook to stable if we thought that security risks and the pressure on domestic economic prospects had lessened.

Hybrids: We do not assign outlooks to bank issue ratings. However, we will continue to notch down the ratings on Mizrahi's hybrids from the SACP. Therefore, we would lower our rating on the bank's rated subordinated instruments if we were to lower the SACP on Mizrahi.

Ratings score snapshot

	To	From
Issuer credit rating	BBB+/Negative/A-2	A-/Negative/A-2
Stand-alone credit profile	bbb+	bbb+
Anchor	bbb	bbb
Business position	Adequate (0)	Adequate (0)
Capital and earnings	Strong (+1)	Strong (+1)
Risk position	Adequate (0)	Adequate (0)
Funding and liquidity	Adequate (0)	Adequate (0)
Comparable ratings analysis	0	0
Support	0	+1
ALAC support	0	0
GRE support	0	0
Group support	0	0
Sovereign support	0	+1
Additional factors	0	0

ALAC--Additional loss-absorbing capacity. GRE--Government-related entity.

Israel Discount Bank Ltd.

Regina Argenio

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We affirmed our rating on IDB because we consider that it is still likely to receive extraordinary government support, if needed, because its stand-alone creditworthiness is weaker than peers. The bank's SACP, which remains at 'bbb', balances IDB's improved operational efficiency and profitability, combined with its resilient asset quality metrics, against the negative effects spilling over from the difficult economic environment.

Outlook

The negative outlook on IDB that further escalation of the war could have negative implications for IDB's creditworthiness over the next 12-24 months.

Downside scenario: We could lower the ratings on IDB if we downgraded Israel as we would consider the government less likely to provide IDB with extraordinary support in case of need. We could also lower the rating if we considered that a structural increase in economic risks in Israel was likely to have negative consequences for the banking sector and IDB's asset quality, capitalization, or earnings.

We could also downgrade IDB if we expected its creditworthiness to weaken, relative to peers. This could happen, for example, if the bank failed to deliver a resilient performance and its asset quality, capitalization, or earnings weakened.

Upside scenario: We could revise the outlook to stable if we revised the outlook on Israel to stable and thought that security risks and the pressure on domestic economic prospects had lessened.

Ratings score snapshot

	To	From
Issuer credit rating	BBB+/Negative/A-2	BBB+/Negative/A-2
Stand-alone credit profile	bbb	bbb
Anchor	bbb	bbb
Business position	Adequate (0)	Adequate (0)
Capital and earnings	Adequate (0)	Adequate (0)
Risk position	Moderate (-1)	Moderate (-1)
Funding and liquidity	Adequate (0)	Adequate (0)
Comparable ratings analysis	+1	+1
Support	+1	+1
ALAC support	0	0
GRE support	0	0
Group support	0	0
Sovereign support	+1	+1
Additional factors	0	0

ALAC--Additional loss-absorbing capacity. GRE--Government-related entity.

Related Criteria

- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, April 30, 2024
- General Criteria: National And Regional Scale Credit Ratings Methodology, June 8, 2023
- General Criteria: Hybrid Capital: Methodology And Assumptions, March 2, 2022
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Dec. 9, 2021
- Criteria | Financial Institutions | General: Financial Institutions Rating Methodology, Dec. 9, 2021
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Israel Long-Term Ratings Lowered To 'A' From 'A+' On Heightened Security Risk; Outlook Negative, Oct. 1, 2024
- Bank Leumi le-Israel B.M., Aug. 1, 2024
- Mizrahi Tefahot Bank Ltd., Aug. 1, 2024
- Various Rating Actions On Israeli Banks On Increased Geopolitical Risks; All Outlooks Negative, May 2, 2024
- Bank Hapoalim B.M., Feb. 8, 2024
- Israel Discount Bank Ltd., Jan. 31, 2024

Ratings List

*****Bank Hapoalim B.M.*****		
Downgraded; Ratings Affirmed		
To		From
Bank Hapoalim B.M.		
Bank Hapoalim B.M. (New York branch)		
Issuer Credit Rating	BBB+/-Negative/A-2	A-/Negative/A-2
Ratings Affirmed		
Bank Hapoalim B.M.		
Junior Subordinated	BBB-	

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***** Bank Leumi le-Israel B.M. *****

Downgraded

	To	From
Bank Leumi le-Israel B.M.		
Senior Unsecured	BBB+	A-

Downgraded; Ratings Affirmed

	To	From
Bank Leumi le-Israel B.M.		
Issuer Credit Rating	BBB+/Negative/A-2	A-/Negative/A-2

Ratings Affirmed

Bank Leumi le-Israel B.M.

Junior Subordinated	BBB-
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***** Israel Discount Bank Ltd. *****

Ratings Affirmed

Israel Discount Bank Ltd.

Issuer Credit Rating	BBB+/Negative/A-2
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Israel Discount Bank of New York

Issuer Credit Rating	BBB+/Negative/--
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***** Mizrahi Tefahot Bank Ltd. *****

Downgraded; Ratings Affirmed

	To	From
Mizrahi Tefahot Bank Ltd.		
Issuer Credit Rating	BBB+/Negative/A-2	A-/Negative/A-2

Ratings Affirmed

Mizrahi Tefahot Bank Ltd.

Junior Subordinated	BBB-
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Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.spglobal.com/ratings for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at <https://disclosure.spglobal.com/ratings/en/regulatory/article/-/view/sourceid/504352>. Complete ratings information is available to RatingsDirect subscribers at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.spglobal.com/ratings. Alternatively, call S&P Global Ratings' Global Client Support line (44) 20-7176-7176.

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