

13 NOV 2024

Fitch Affirms Israel Discount Bank at 'A-'; Outlook Negative

Fitch Ratings - London - 13 Nov 2024: Fitch Ratings has affirmed Israel Discount Bank Limited's (IDB) Long-Term Issuer Default Rating (IDR) at 'A-' with a Negative Outlook and Short-Term IDR at 'F1'. The bank's Viability Rating (VR) has been affirmed at 'a-'.

Key Rating Drivers

VR and Support Drive Ratings: IDB's Long-Term IDR is driven by its VR and underpinned by our view of a very high probability that Israel (A/Negative/F1+) would provide support to IDB, if needed. Fitch assesses Israel's ability and propensity to support IDB as very high, particularly given the bank's systemic importance in the country, with about 15% of banking system assets.

Universal Banking Franchise: IDB's VR reflects a good domestic universal banking franchise, improved asset quality and profitability, and adequate capitalisation and funding. IDB is required to reduce its shareholdings in its credit card subsidiary, Israel Credit Cards Ltd. (Cal), to improve competition. It has also announced the sale of a minority stake in its US subsidiary bank. However, these actions do not significantly change our view of IDB's business profile.

High Loan Growth: The bank has grown its mortgage book in recent years, taking market share from competitors, but we view this segment as lower risk due to conservative underwriting standards as a result of prudent regulatory limits and close oversight. IDB has also increased construction and real estate lending, a higher-risk subsector, although demand is driven by high population growth, which supports housing credit demand and mitigates risks.

Sound Asset Quality: Impaired loans were 0.8% of gross loans at end-1H24, which compares favourably with both domestic and international peers. Loan growth has been high in recent years, so we expect higher loan impairment charges as new loans season. We also expect the impaired loans ratio to be slightly higher than domestic peers through the cycle as long as IDB owns a credit card subsidiary, but to remain below 1.5% over the next two years.

Growth, Higher Rates Benefit Earnings: Net interest income has benefited from interest-rate rises and higher loan volumes in recent years. Operating profitability, which has historically been lower than peers', is benefiting from improved cost efficiency, with a Fitch-calculated cost/income ratio of 52% in 1H24, compared with an average of 68% over the past decade. We expect operating profit to continue to benefit from net interest income, due to higher interest rates and improving cost controls.

Adequate Capital Buffers: Headroom in our assessment is limited, but capitalisation has remained

adequate, with a 10.67% common equity Tier 1 (CET1) ratio at end-1H24 versus its 9.19% minimum regulatory requirement. We expect the bank to manage its capitalisation proactively, particularly during periods of high growth, and to maintain the current buffers over regulatory requirements.

Our capitalisation assessment also considers the bank's improved internal capital generation and its fairly high ratio of risk-weighted assets (RWA) to total assets (end-1H24: 72%), as the bank uses the standardised approach to calculate credit-risk RWAs.

Sound Funding and Liquidity: IDB's 91% loans/deposits ratio is higher than its largest domestic peers, but broadly in line with international peers. Funding benefits from the bank's stable and granular deposit base, split equally between retail and corporate deposits. Liquidity is sound, with a liquidity coverage ratio of 133% at end-1H24.

IDB's 'F1' Short-Term IDR is the higher of two possible Short-Term IDRs that map to a 'A-' Long-Term IDR. This is because we view the sovereign's propensity to support as more certain in the near term.

Rating Sensitivities

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade

A downgrade of the sovereign ratings would result in a downgrade of IDB's Long-Term IDR and senior debt ratings if accompanied by a downgrade of the bank's VRs.

A sharp increase in the bank's risk environment that increases the likelihood of asset quality deterioration could result in a downgrade. A deterioration of asset quality that results in an impaired loan ratio of above 2% for an extended period, combined with the CET1 declining below current levels and weakening internal capital generation, could also result in a VR downgrade. Given the bank's significant exposure to the real estate sector, a sharp decline in real estate prices would put pressure on asset quality, and therefore on the VR.

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

An upgrade of IDB's IDRs is unlikely due to the Negative Outlook on the sovereign's Long-Term IDR. We would revise the Outlook to Stable if the sovereign Outlook was revised to Stable.

An upgrade of IDB's VR is unlikely given the bank's geographical concentration and would require a material and structural improvement in profitability that allows the bank to generate stronger and more stable operating profit/RWAs ratio, while also maintaining materially higher capital ratios, which we do not expect.

OTHER DEBT AND ISSUER RATINGS: KEY RATING DRIVERS

IDB's senior unsecured notes are rated in line with the Long-Term IDR. This reflects our view that a default on senior unsecured debt equates to a default of the bank. It also reflects Fitch's expectation of average recovery prospects.

The Long-Term IDR (xgs) of 'A-(xgs)' is at the level of the VR. The Short-Term IDR (xsg) of 'F2(xgs)' is the lower of two possible options that map to a 'A-' Long-Term IDR (xgs) due to IDB's 'a-' funding & liquidity score.

OTHER DEBT AND ISSUER RATINGS: RATING SENSITIVITIES

The rating on the senior unsecured notes is sensitive to a change in the bank's IDR.

The IDRs (xgs) are sensitive to changes in the bank's VR.

VR ADJUSTMENTS

The operating environment score has been assigned below the implied score due to the following adjustment reasons: sovereign rating (negative), size and structure of economy (negative)

The business profile score has been assigned above the implied score due to the following adjustment reason: market position (positive)

The capitalisation & leverage score has been assigned above the implied score due to the following adjustment reason: leverage and risk-weight calculation (positive).

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

Public Ratings with Credit Linkage to other ratings

IDB's IDRs and Government Support Rating reflect a very high probability of support from Israel.

ESG Considerations

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit <https://www.fitchratings.com/topics/esg/products#esg-relevance-scores>.

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Rating Actions

ENTITY/DEBT	RATING		RECOVERY		PRIOR
Israel Discount Bank Limited	LT IDR	A- 	Affirmed		A- 
	ST IDR	F1	Affirmed		F1
	Viability	a-	Affirmed		a-
	Government Support	a-	Affirmed		a-
	LT IDR (xgs)	A-(xgs)	Affirmed		A-(xgs)
	ST IDR (xgs)	F2(xgs)	Affirmed		F2(xgs)
	• senior unsecured LT	A-	Affirmed		A-

ENTITY/DEBT	RATING	RECOVERY	PRIOR
• senior unsecured	LT (xgs) A-(xgs)	Affirmed	A-(xgs)

RATINGS KEY OUTLOOK WATCH

POSITIVE	⊕	◆
NEGATIVE	⊖	◆
EVOLVING	⊕	◆
STABLE	⊙	

Applicable Criteria

[Bank Rating Criteria \(pub.15 Mar 2024\) \(including rating assumption sensitivity\)](#)

Additional Disclosures

[Solicitation Status](#)

Endorsement Status

Israel Discount Bank Limited UK Issued, EU Endorsed

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