

Midroog Rating Scales and Definitions

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PREFACE

This document presents the rating scales used at Midroog as well as various definitions related to credit ratings and Midroog's other non-credit ratings products. The purpose of this document is to create transparency in respect to those scales and definitions and to present them as clearly and simply as possible.

CREDIT RATINGS SCALES

Credit ratings are assigned to issuers, obligations or financial instruments on Midroog's local rating scales and are forward-looking opinions of their creditworthiness, relative to other local issuers.

Midroog defines creditworthiness as the issuer's ability to meet its contractual obligations (probability of default) and loss in the event of default or impairment (loss given default), the combination of both can be referred to as expected loss.

Midroog aspires to reflect in its credit ratings the expected loss by an ordinal (relative) ranking, i.e. the expected loss at lower ratings will be higher than the expected loss at higher ratings¹. Midroog's opinion regarding creditworthiness, as defined above, is expressed on all points in Midroog's rating scale.

However, usually, Midroog does not include either probability of default or loss given default as distinct quantitative values in its rating process. Rather, it assesses the issuer's ability to meet its obligations and recovery in the event of default or impairment, relative to other rated issuers using the parameters listed in rating methodologies.

In addition, in ratings of various financial instruments, Midroog factors in their specific characteristics, that could influence the level of the expected *loss given default*², even if it does not make a quantitative estimate of loss given default, unless there was a default event. In order to reflect the difference in expected loss within the capital structure (reflecting each specific instrument's characteristics), the expected loss and thus the rating of financial instrument may deviate from the issuer rating.

Regarding ratings assigned to preferred shares or other hybrid instruments, in which payment default is not defined, or does not match investor expectations of timely payment, those ratings reflect the probability of impairment and the expected loss in the event of impairment. For definitions of impairment, see hereinbelow.

Since Midroog's credit ratings address expected loss, Midroog's credit ratings analysis of debt instruments or issuers in default and impaired instruments (i.e. issuers of debt instruments for which the likelihood of default is assessed as certain or very material, since they are already in default or considered highly likely to default), includes the recovery rate as a key element in its analysis.

¹ Ratings of certain financial instruments such as various types of subordinate debts are determined relative to the issuer rating (i.e. a certain number of notches lower than the issuer's rating).

² Characteristics such as the security's degree of seniority, support/collateral, and the instrument's various terms may affect the rating, based on the considerations set forth in the relevant rating methodologies.

The financial instruments addressed by Midroog's ratings are those that require payment of an ascertainable amount, which may vary based upon standard sources of variation (such as variable interest and/or linkage to the CPI) by an ascertainable date, without regard to enforceability³. Midroog's ratings do not address non-standard sources of variation regarding the amount of the principal obligation (such as linkage to an equities index), unless otherwise stated in its initial rating report⁴.

Long-term ratings are assigned to issuers, obligations or financial instruments with an original maturity of more than one year. Short-term ratings are assigned to issuers, obligations or financial instruments with an original maturity of up to and including one year. For the short-term rating scale, see hereinbelow.

³ For issuer ratings, see the definition below. In certain cases, creditworthiness relates to a third party in addition to or instead of the issuer. For example: credit linked notes or guaranteed instruments.

⁴ Midroog does not classify the various types of non-standard sources of variation, because the types of characteristics of financial instruments is unlimited. Examples of such sources include: various indices, equity value and cash flow, prepayment penalties and a payment obligation not defined at the onset of the transaction. For further details on the types of hybrid instruments we rate, see the methodology report on Midroog's website, www.midroog.co.il.

Local Long-Term Rating Scale

Aaa.il	Issuers or issues rated Aaa.il are those that, in Midroog's judgment, have highest creditworthiness relative to other local issuers.
Aa.il	Issuers or issues rated Aa.il are those that, in Midroog's judgment, have very strong creditworthiness relative to other local issuers.
A.il	Issuers or issues rated A.il are those that, in Midroog's judgment, have high creditworthiness relative to other local issuers.
Baa.il	Issuers or issues rated Baa.il are those that, in Midroog's judgment, have moderate creditworthiness relative to other local issuers, and could involve certain speculative characteristics.
Ba.il	Issuers or issues rated Ba.il are those that, in Midroog's judgment, have weak creditworthiness relative to other local issuers, and involve speculative characteristics.
B.il	Issuers or issues rated B.il are those that, in Midroog's judgment, have very weak creditworthiness relative to other local issuers, and involve significant speculative characteristics.
Caa.il	Issuers or issues rated Caa.il are those that, in Midroog's judgment, have extremely weak creditworthiness relative to other local issuers, and involve very significant speculative characteristics.
Ca.il	Issuers or issues rated Ca.il are those that, in Midroog's judgment, have extremely weak creditworthiness ability and are likely very near default, with some prospect of recovery of principal and interest.
C.il	Issuers or issues rated C are those that, in Midroog's judgment, have the weakest creditworthiness and are usually in a situation of default, with little prospect of recovery of principal and interest.

Note: Midroog appends numeric modifiers 1, 2, and 3 to each rating category from Aa.il to Caa.il. The modifier '1' indicates that the obligation ranks in the higher end of its rating category, which is denoted by letters. The modifier '2' indicates that it ranks in the middle of its rating category and the modifier '3' indicates that the obligation ranks in the lower end of that category, denoted by letters.

Note: For more information on long-term ratings assigned to obligations in default or to impaired debt, see the definitions below in this publication.

Additionally, a (hyb) modifier is added to all ratings of hybrid securities issued by banks and insurers. By their terms, hybrid securities allow for the omission of scheduled dividends, interest, or principal payments, which could potentially result in impairment⁵ if such an omission occurs. Hybrid securities may also be subject to contractually allowable write-downs of principal that could result in impairment. A long-term rating with a (hyb) indicator reflects the relative credit risk associated with that security. For more information on using the (hyb) indicator, see the document "The (hyb) indicator in rating financial instruments of banks and insurance companies" on Midroog's website at www.midroog.co.il.

⁵ For a definition of impaired debt, see below in this publication.

Local Short-Term Rating Scale

P-1.il	Issuers rated Prime-1.il are, in Midroog's judgment, have very good ability to repay short-term obligations relative to other local issuers.
P-2.il	Issuers rated Prime-2.il are, in Midroog's judgment, have good ability to repay short-term obligations relative to other local issuers.
P-3.il	Issuers rated Prime-3.il are, in Midroog's judgment, have moderate ability to repay short-term obligations relative to other local issuers.
NP.il	Issuers rated Not Prime.il do not, in Midroog's judgment, belong in any of the above three Prime categories.

Linkage between the Long-Term and Short-Term Rating Scales

The following table shows the long-term ratings consistent with short-term ratings, when such long-term ratings exist⁶⁷.

Long Term Rating	Short Term Rating
Aaa.il Aa1.il Aa2.il Aa3.il A1.il A2.il	→ Prime-1.il
A3.il Baa1.il Baa2.il	→ Prime-2.il
Baa3.il	→ Prime-3.il
Ba1.il, Ba2.il, Ba3.il B1.il, B2.il, B3.il Caa1.il, Caa2.il, Caa3.il Ca.il C.il	→ Not Prime

⁶ In accordance with and subject to the "Short Term Rating" methodology. See on Midroog's website.

⁷ Structured finance short-term ratings are usually based on the short-term rating of a liquidity provider for the transaction or an assessment of cash flows available to repay the rated obligation.

Types of Obligations and Issuers Rated on the Long-Term and Short-Term Scales

Long-Term and Short-Term Obligations

Midroog assigns ratings to long-term obligations and to short-term obligations. Long-term ratings are assigned to issuers or obligations or to financial instruments with an original maturity of a year or more and reflect Midroog's opinion on the likelihood of a default or impairment on contractual financial obligations and the expected financial loss suffered in the event of default or impairment, relative to other local issuers. Short-term ratings are assigned to issuers or obligations or to financial instruments with original maturity up to a year and reflect Midroog's view creditworthiness with respect to short-term obligations relative to other local issuers. The opinion on creditworthiness derived from the long-term rating and its implications for the issuer's ability to meet its short-term obligations and explanations of these definitions are set forth in full in the short-term rating methodology "short-term ratings" published on Midroog's website.

Bank Deposit Ratings

Bank deposit ratings are Midroog's assessment of a bank's ability to repay deposits. In long-term deposit ratings, the assessment also reflects the expected loss given default.

Credit Default Swap Ratings

CDS ratings assess the risk associated with the obligations that a credit protection provider has with respect to credit events under the terms of the transaction. The ratings do not address potential losses resulting from early termination of the transaction, nor market risks associated with the transaction.

Insurance Financial Strength Rating

An Insurance Financial Strength Rating is Midroog's assessment of an insurer's ability to fulfill its obligations to policy holders. The rating also reflects the expected loss given default.

Issuer Ratings

An issuer rating is Midroog's assessment of the issuer's ability to repay its senior, unsecured financial obligations. Issuer ratings incorporate external support that is expected to apply to all the issuer's senior unsecured financial obligations, such as: explicit support arising from guarantees of all senior unsecured obligations and/or implied support for issuers subject to joint default analysis (for example, banks and government-related issuers). An issuer rating does not incorporate support arrangements, such as guarantees, that apply only to specific (but not all) senior unsecured obligations.

ADDITIONAL RATINGS AND SYMBOLS

Structured Finance Ratings

Midroog differentiates between structured finance ratings and all other ratings (such as corporate ratings, ratings of financial institutions, government related issuers) by adding the indicator (sf) to structured finance ratings. The purpose of adding the modifier is to eliminate any presumption that structured finance ratings and other ratings at the same rating level will behave the same, and to clarify that the risk characteristics of these securities may differ. However, through implementing its rating methodologies, Midroog aspires to achieve a broad equivalence in the performance of structured finance and other ratings in the long run⁸. For more details on using the (sf) indicator, see the document "The (sf) indicator in structured finance ratings" on Midroog's website at www.midroog.co.il.

Provisional Ratings

Midroog assigns provisional ratings to issuers or financial instruments, when the assignment of definitive rating is subject to the fulfillment of contingencies that could affect the rating. Examples of such contingencies are final documents or the fulfillment of conditions, when the rating is sensitive to changes to the final conditions. When such contingencies are not present, a definitive rating may be assigned based upon documentation that is not yet in final form. The symbol (P)⁹ is removed when the applicable contingencies have been fulfilled.

Withdrawing a Rating

When Midroog no longer rates an issuer, an obligation or a financial instrument on which it had previously maintained a rating, the symbol WR is employed.

⁸ Like other ratings, structured finance ratings reflect both the likelihood of a default, and the expected loss suffered in the event of default. Ratings are assigned based Midroog's assessment of a security's expected loss rate (default probability multiplied by expected loss severity), and may be subject to the constraint that the final rating assigned would not be more than a certain number of notches (typically three to five notches), above the rating that would be assigned based on an assessment of default probability alone. The considerations affecting the scale of this constraint will typically include the level of the rating, the seasoning of the transaction and the level of uncertainty in the assessment of the expected loss and the probability of default.

⁹ Provisional

Managed Linked Certificate (MLC) Ratings

A MLC rating is Midroog's assessment of an issuer's ability to repay obligations to holders of MLCs, in accordance with its obligations in the relevant transaction documentation (such as: prospectus, trust deed, shelf offering report, etc.). The rating reflects Midroog's assessment the issuer will not have sufficient assets at the relevant time to redeem the MLCs (i) to the relevant value of the tracked financial asset/s or index; or (ii) in the form of the actual financial asset/s (as applicable), net of management fees and conversion fees, in accordance with the terms of the relevant transaction documentation. To remove any doubt, the rating does not refer to the returns or losses on the MLC resulting from changes in the relevant index or financial asset/s. The symbol ^{MLC}, indicating that the rating is of a MLC, will be added to the regular rating symbol.

Managed Linked Certificate Rating Scale

Aaa^{MLC}	Obligations rated Aaa ^{MLC} are those that, in Midroog's judgment, have the highest repayment ability relative to other local obligations.
Aa^{MLC}	Obligations rated Aa ^{MLC} are those that, in Midroog's judgment, have very high repayment ability relative to other local obligations.
A^{MLC}	Obligations rated A ^{MLC} are those that, in Midroog's judgment, have relatively high repayment ability relative to other local obligations.
Baa^{MLC}	Obligations rated Baa ^{MLC} are those that, in Midroog's judgment, have relatively moderate repayment ability relative to other local obligations, and could have certain speculative characteristics.
Ba^{MLC}	Obligations rated Ba ^{MLC} are those that, in Midroog's judgment, have relatively weak repayment ability relative to other local obligations, and have speculative characteristics.
B^{MLC}	Obligations rated B ^{MLC} are those that, in Midroog's judgment, have very weak repayment ability relative to other local obligations, and have significant speculative characteristics.
Caa^{MLC}	Obligations rated Caa ^{MLC} are those that, in Midroog's judgement, have the weakest repayment ability relative to other local obligations, and have very significant speculative characteristics.
Ca^{MLC}	Obligations rated Ca ^{MLC} are those that, in Midroog's judgement, have extremely weak repayment ability and are very near default, with some prospect of repaying obligations.
C^{MLC}	Obligations rated C ^{MLC} are those that, in Midroog's judgment, have the weakest repayment ability and are usually in default, with little prospect of repaying obligations.

Note: Midroog appends numeric modifiers 1, 2, and 3 to each rating category from Aa^{MLC} to Caa^{MLC}. The modifier '1' indicates that the obligation ranks in the higher end of its rating category, which is denoted by letters. The modifier '2' indicates that it ranks in the middle of its rating category and the modifier '3' indicates that the obligation ranks in the lower end of that category, denoted by letters.

Index Linked Certificate (ILC) Notes Ratings

An ILC Notes Rating is assigned with respect to a bond/obligation linked to a specific tracked index, including interest rates and currency rates and reflects Midroog's assessment of an issuer's ability to repay note holders principal and interest (as applicable) on time and in accordance with the conditions set in the transaction documents. The rating does not address market risk (i.e. it does not reflect e.g. potential decreases in the amount of the principal obligation or yields). The symbol ^{ILC} indicating that the rating is of ILC Notes, will be added to the regular rating symbol.

Index Linked Certificate (ILC) Notes Rating Scale

Aaa^{ILC}	Notes rated Aaa ^{ILC} are those that, in Midroog's judgment, have the highest repayment ability relative to other local obligations.
Aa^{ILC}	Notes rated Aa ^{ILC} are those that, in Midroog's judgment, have very high repayment ability relative to other local obligations.
A^{ILC}	Notes rated A ^{ILC} are those that, in Midroog's judgment, have relatively high repayment ability relative to other local obligations.
Baa^{ILC}	Notes rated Baa ^{ILC} are those that, in Midroog's judgment, have relatively moderate repayment ability relative to other local obligations, and could have certain speculative characteristics.
Ba^{ILC}	Notes rated Ba ^{ILC} are those that, in Midroog's judgment, have relatively weak repayment ability relative to other local obligations, and have speculative characteristics.
B^{ILC}	Notes rated B ^{ILC} are those that, in Midroog's judgment, have very weak repayment ability relative to other local obligations, and have significant speculative characteristics.
Caa^{ILC}	Notes rated Caa ^{ILC} are those that, in Midroog's judgment, have the weakest repayment ability relative to other local obligations, and have very significant speculative characteristics.
Ca^{ILC}	Notes rated Ca ^{ILC} are those that, in Midroog's judgment, have extremely weak repayment ability and are very near default, with some prospect of repaying interest and principal.
C^{ILC}	Notes rated C ^{ILC} are those that, in Midroog's judgment, have the weakest repayment ability and are usually in default, with little prospect of repaying interest and principal.

Note: Midroog appends numeric modifiers 1, 2, and 3 to each rating category from Aa^{ILC} to Caa^{ILC}. The modifier '1' indicates that the obligation ranks in the higher end of its rating category, which is denoted by letters. The modifier '2' indicates that it ranks in the middle of its rating category and the modifier '3' indicates that the obligation ranks in the lower end of that category, denoted by letters.

Indicative Ratings

An indicative rating is a point-in-time opinion of the potential credit rating of an issuer, or proposed debt issuance by an issuer contemplating such a debt issuance at some future date. Indicative ratings are not equivalent to and do not represent regular credit ratings and further assessment and/or information is required in order to determine a regular credit rating. An indicative rating is unmonitored, confidential, intended for the internal use of the commissioner of the rating and not intended for publication. Indicative ratings are applicable to issuers or financial instruments that are not rated by Midroog at the time the indicative rating is given.

RELATIVE SCORES FOR OTHER ASSETS AND SERVICES

Investment Manager Quality (MQ) Assessments

Investment Manager Quality Assessment of Asset Managers ("MQ Assessment") are forward-looking opinions of the manner in which asset managers (i.e. entities whose main business includes investment and asset management and yielding returns for others) manage investments, relative to others. MQ Assessments do not indicate an asset manager's ability to repay a fixed financial obligation or satisfy contractual financial obligations, neither those entered by the manager nor any that may have been entered into through actively managed portfolios. The MQ Assessment also does not examine or evaluate the expected returns or losses, asset value and volatility of assets and does not constitute a credit rating.

An MQ Assessment examines and provides an opinion regarding the quality of the asset manager's management characteristics, in accordance with the following definitions:

MQ1.il	The quality of investment management by asset manager is assessed to be very high, based on weighting management characteristics, compared with other local entities.
MQ2.il	The quality of investment management by asset manager is assessed to be high, based on weighting management characteristics, compared with other local entities.
MQ3.il	The quality of investment management by asset manager is assessed to be moderate, based on weighting management characteristics, compared with other local entities.
MQ4.il	The quality of investment management by asset manager is assessed to be adequate, based on weighting management characteristics, compared with other local entities.
MQ5.il	The quality of investment management by asset manager is assessed to be weak, based on weighting management characteristics, compared with other local entities.

ANCILLARY SERVICES

Rating Assessment Service

The Rating Assessment Service or RAS is an opinion relating to the potential credit rating, or of the potential impact on an existing credit rating, given one or more concrete hypothetical scenario provided to Midroog in writing by the entity requesting the service. The Rating Assessment is confidential, unpublished and intended for the customer's internal use. It is unmonitored and point-in-time. Rating Assessments are not equivalent to and do not represent traditional credit ratings. Should a credit rating be determined at a later date following materialization of the scenario, the level of the rating may differ from that of the rating assessment.

A scenario is (1) a proposed transaction/project and/or debt issuance that materially alters the issuer's current state (including acquisitions, disposals, share buybacks, listings, initial public offerings, and material restructuring) or (2) a proposed initial transaction/project and/or debt issuance; or a materially different variation on any such transaction/project and/or debt issuance, including a material change in the overall size of the debt being contemplated.

Rating Forecasts

A Rating Forecast is an unpublished, point-in-time preliminary opinion on the approximate creditworthiness of an unrated entity or a financial obligation of an unrated entity, referring to the general credit strengths and weaknesses of an obligor relative to peers. Although Rating Forecasts are expressed on Midroog's credit rating scale, they are not credit ratings and are not assigned by rating committees. Had Midroog conducted an analysis commensurate with a full rating, the result may have been significantly different. It should be noted that Midroog will report data received in connection with requests for rating forecasts in its annual report, where required to do so by applicable Israeli regulations¹⁰ regulating credit rating companies.

Servicer Quality (SQ) Assessments

An SQ Assessment is Midroog's assessment of the operational quality of servicers' loan servicing practices. This assessment does not address the credit quality of the assets the servicer handles. Note that as of the writing of this document, Midroog carries out SQ assessments as part of the process of rating certain financial instruments.

Originator Assessments (OA)

Originator assessments are Midroog's assessments of the operational quality of originators' loan origination practices. Note that as of the writing of this document, Midroog carries out OA assessments as part of the process of rating certain financial instruments.

¹⁰ Regulations Regulating the Activity of Credit Rating Companies 5774-2014.

ASSESSMENTS USED AS INPUTS INTO RATINGS

These Assessments do not constitute credit ratings. The manner in which these assessments are used is described in the relevant rating methodologies in which they are used.

Credit Estimates

A Credit Estimate is an unpublished point-in-time opinion of the approximate credit quality of an obligation, financial instrument or issuer. Although Credit Estimates are expressed using Midroog's credit rating scale, Credit Estimates are not equivalent to and do not represent regular credit ratings.

Had Midroog conducted an analysis commensurate with a full Midroog credit rating, the result may have been significantly different. Also, Credit Estimates are unmonitored, however they may be updated from time to time. Credit Estimates are usually based on public information or third-party information, without the issuer taking part in the process. Credit Estimates serve as inputs for regular credit ratings and are expressed on Midroog regular rating scales.

Baseline Credit Assessment (BCA)

BCAs are Midroog's assessments of issuers' standalone intrinsic financial strength, absent extraordinary external support from an affiliated company¹¹ or the state.

The BCA represents an assessment of the likelihood of an issuer requiring extraordinary external support in order to avoid default of one or more of its obligations, or the likelihood of the default absent such extraordinary support. The BCA does not address the expected loss in the event that external support is not provided.

Contractual relationships between a government or an affiliate and a supported issuer and any expected ongoing annual subsidies from the government or an affiliate are incorporated in BCAs and are therefore considered intrinsic to the issuer's standalone financial strength. Extraordinary support is typically idiosyncratic in nature and is meant to avoid default by the issuer.

The BCA is denoted by lower-case letters in an alphanumeric rating scale, that corresponds to the alphanumeric long-term rating scale.

¹¹ An affiliate includes parent, cooperative groups, and significant investors (typically greater than 20% of the voting interest). Government includes local, regional and national government.

Baseline Credit Assessment scale

aaa.il	Issuers and issues assessed at aaa.il are those that, in Midroog's judgment, have the highest internal or independent financial strength, relative to other local issuers, absent any possibility of extraordinary support from an affiliate or the government.
aa.il	Issuers and issues assessed at aa.il are those that, in Midroog's judgment, have very high internal or independent financial strength, relative to other local issuers, absent any possibility of extraordinary support from an affiliate or the government.
a.il	Issuers and issues assessed at a.il are those that, in Midroog's judgment, have relatively high internal or independent financial strength, relative to other local issuers, absent any possibility of extraordinary support from an affiliate or the government.
baa.il	Issuers and issues assessed at baa.il are those that, in Midroog's judgment, have moderate internal or independent financial strength, relative to other local issuers, absent any possibility of extraordinary support from an affiliate or the government, and may have certain speculative characteristics.
ba.il	Issuers and issues assessed at ba.il are those that, in Midroog's judgment, have relatively weak internal or independent financial strength, relative to other local issuers, absent any possibility of extraordinary support from an affiliate or the government, and have speculative characteristics.
b.il	Issuers and issues assessed at b.il are those that, in Midroog's judgment, have very weak internal or independent financial strength, relative to other local issuers, absent any possibility of extraordinary support from an affiliate or the government, and have significant speculative characteristics.
caa.il	Issuers and issues assessed at caa.il are those that, in Midroog's judgment, have extremely weak internal or independent financial strength, relative to other local issuers, absent any possibility of extraordinary support from an affiliate or the government, and have very speculative characteristics.
ca.il	Issuers and issues assessed at ca.il are those that, in Midroog's judgment, have extremely weak internal or independent financial strength, relative to other local issuers, absent any possibility of extraordinary support from an affiliate or the government, and are very near default, with some prospect of recovery of principal and interest.
c.il	Issuers and issues assessed at c.il are those that, in Midroog's judgment, have the weakest internal or independent financial strength, relative to other local issuers, absent any possibility of extraordinary support from an affiliate or the government, and are usually in default, with little prospects of recovery of principal and interest.

Note: Midroog appends numeric modifiers 1, 2, and 3 to each rating category from aa.il to caa.il. The modifier '1' indicates that the debenture ranks in the higher end of its rating category, which is denoted by letters. The modifier '2' indicates that it ranks in the middle of its rating category and the modifier '3' indicates that the debenture ranks in the lower end of that category, denoted by letters.

OTHER DEFINITIONS

Rating outlook

A rating outlook is Midroog's assessment of the likely rating direction over the medium term. Rating outlooks fall into four categories: positive, stable, negative or developing. Rating outlooks can be set at the level of the issuer or the obligation. The modifier "m" (multiple) is added when different obligations of the same issuer have different outlooks. The rationale for the differential in rating outlooks in these cases shall be explained in the rating reports. Rating outlooks are not assigned to all ratings. Cases where no outlook is set are indicated by the modifier NOO (no outlook).

A stable outlook reflects low expectations of a rating change over the medium term. A positive, negative or developing outlook reflects a higher likelihood of change over the medium term. When assigning the outlook, the rating committee is indicating its belief that the credit repayment ability of the issuer is consistent with the relevant rating level at that point in time.

In the event that a rating changes in the direction indicated by the outlook, the time between the determination of that outlook and the relevant change in the rating varies widely depending on the pace of developments relating to assessed credit risk and the significance of their impact on Midroog's view of the issuer's credit repayment ability. On average, the time between a change in outlook and a change in the relevant rating outlook and/or rating is generally longer when the rating is assigned a stable outlook and shorter when the rating is assigned any other outlook.

For statistics on changes in ratings in the periods after an outlook is assigned and the average duration of rating outlooks, see [rating performance reports](#) on the Midroog website.

Credit review

When a rating is placed under credit review, its rating may change in the near term. A rating review may be carried out to upgrade a rating – credit review with positive implications, downgrade it – credit review with negative implications and in certain cases, with uncertain direction – credit review with direction uncertain. The review may end with an upgrade, downgrade or unchanged rating.

Ratings are placed on credit review when a change in rating and/or rating outlook may be warranted in the near term, but more information or further analysis are required in order to reach any decision on changing the rating, or the magnitude of the change.

The near term could be immediate or could be within the several months following the placing of the rating on review. However, the time a rating is under review often lasts for a longer period.

The time between the origination of a rating review and its completion varies widely, depending on the circumstances of the review and the time required to obtain the information relevant to determining the rating and analyzing that information. In some cases, the ability to complete the rating review depends on the occurrence (or non-occurrence) of a specific event, the timing of which Midroog cannot control. In such cases and other unique situations, there may be greater uncertainty regarding the time until the rating review is completed.

For statistics on the changes in ratings after their placement on credit review and duration of credit reviews, see [rating performance reports](#) on the Midroog website.

Definition of default

Midroog's definitions for default apply only to debt or debt-like obligations (such as CDS). Three events constitute a debt default¹²:

- (1) A missed or delayed disbursement of a contractually obligated interest or principal payment (excluding missed payments cured within a contractually allowed grace period).
- (2) A court filing in respect to bankruptcy proceedings of the issuer, such as: bankruptcy filing, temporary bankruptcy, receivership or Chapter 11. While it is likely to cause a miss or delay in expected planned debt service payments.
- (3) A debt arrangement or restructuring proposal, whereby a) an obligor offers bondholders new bonds or securities with new terms, whose terms have been redefined, or a package of securities, cash or assets that amount to a diminished financial obligation relative to the original obligation and b) the arrangement has the effect of allowing the obligor to avoid a default¹³.

The definition of default does not include so-called "technical defaults", such as violations of leverage or coverage ratios, unless the obligor fails to cure the violation and fails to honor the resulting debt acceleration which may be required. For the purpose of defining default, also excluded are payments owed on long-term obligations which are missed due to purely technical or administrative errors which are (1) not related to the ability or willingness to make the payments and (2) are cured in very short order (typically, 1-2 business days following discovery of the error).

Also, under some circumstances, missed contractually obligated payments could be excluded if nonpayment resulted from a legal dispute over the validity of the contracts.

Midroog does not view a contractually allowable deferral of interest payment as a default. If however, for a structured finance instrument, the unpaid interest payment is not cured by maturity (or for an instrument whose rating is withdrawn before maturity, if at the time of withdrawal, the payment is not cured nor expected to be cured by maturity), Midroog will at that time consider it as a default.

¹² For certain bonds that give investors dual recourse against both the issuer and a guarantor of the issuer's debt, no event will be considered a debt default unless it occurs in relation to both the issuer's obligations and the guarantor's obligations.

¹³ Midroog includes debt arrangement and restructuring proposals in our definition of default in order to capture credit events whereby issuers effectively fail to meet their debt service obligations but do not actually file for bankruptcy or miss an interest or principal payment. Midroog employs fundamental analysis in assessing the likelihood of future default and considers various indicators in assessing loss relative to the original promise, which may include the yield to maturity of the debt being exchanged.

Definition of Impaired Instrument

An instrument is impaired when investors receive (or expect to receive, with near certainty) less value than would be expected if the obligor were not experiencing financial distress or was otherwise prevented from making payments by a third party, even if the financing documents or trust deed do not allow the investors to act against the obligor in such events, such as resorting to legal bankruptcy proceedings.

Midroog's definitions for impairment, relating to preferred shares and other hybrid securities. An instrument is deemed to be impaired if:

(1) Contractually allowable payment omissions of scheduled dividends, interest or principal payments on preferred shares or other hybrid instruments.

(2) Arrangement (or restructuring of impaired instruments)¹⁴, preferred stock or other hybrid instruments due to financial distress whereby (a) the principal promised to an investor is reduced according to the terms of the instrument or (b) the obligor offers holders new securities or securities whose terms have been redefined or a new package of securities, cash or assets, in order to avoid a contractually-allowable payment omission as described in (1) above.

The definition of an instrument as impaired may change over time if it migrates from impaired to cured (e.g., if initially deferred cumulative preferred dividends are ultimately paid in full) and could also change back again to impaired.

Excluded from impairment events are (1) missed payments due to purely technical or administrative errors which are not related to the ability or willingness to make the payment and (2) are cured in very short order (typically, 1-2 business days).

¹⁴ Impaired debt arrangements are similar to debt arrangements that are part of the definition of default, but impaired debt arrangements are meant to avoid an impairment event, not a default event.

Rating methodologies (Assessment methods)

Rating methodologies describe the analytical framework Midroog rating committees use to assign credit ratings. They set out the main parameters that in Midroog's opinion are key to assessing the creditworthiness of issuers in a certain sector. The methodologies do not constitute exhaustive treatments of all parameters reflected in Midroog ratings, but list key quantitative and qualitative considerations used in determining ratings. In order to create transparency in respect to Midroog's analytical approach in setting ratings, all methodologies are published on Midroog's website.

Methodologies relating to corporates and financial institutions usually make use of rating matrices. A rating matrix is a rating tool that incorporates the main parameters for assigning ratings. It is a summary that does not necessarily contain every rating consideration. The weight for each parameter represents an approximation of their importance for rating decisions. In this context, it bears noting that the actual importance of each factor may vary significantly depending on the circumstances of the issuer and the environment in which it operates. The rating committee applies its own judgment in determining the importance of the rating factors and their examination, for example, the use of forecasts versus past performance. As a consequence of these considerations, assigned ratings may be different than indicated by the ratings matrix.

Methodologies governing structured finance ratings usually make use of rating model/s. A structured finance ratings model is a rating tool that includes the main parameters considered to estimate the distribution of losses for the collateral assets, or to determine the effect on the credit risk of different tranches of bonds depending on expected cash flow from the underlying assets, capital structure, and reserve funds. While methodologies contain fixed values for key parameters to be applied to all issuers in a sector, rating committee employs judgment in determining model inputs, and rating committee considerations may be different than model-indicated outputs.

While most methodologies relate to a particular sector or types of transactions, there are also cross-sector methodologies that have implications for a number of sectors, such as: short-term ratings.

Key Rating Assumptions

Methodologies may (but need not) contain separately identifiable key rating assumptions.

Key rating assumptions are the fixed inputs or range of values described in rating methodologies, such as mathematical or correlation assumptions relevant to an entire sector or certain sectors, or common to multiple credit rating methodologies, and which are part of the considerations of rating committee when assigning ratings. Key rating assumptions are subject to the same governance process as the methodology to which they relate, including the need for changes to be approved by the credit policy committee within Midroog.

By nature, key rating assumptions are relatively timeless inputs to the rating process, and because they seek to bring a degree of stability, consistency and transparency to something that may in practice be uncertain, they are intended to be reasonably resilient to change. They may change overtime in response to long-term structural changes or as more is learned about long-run mutual relationships between risk factors, but they would be very unlikely to change as a result of a short-run change in economic or financial market conditions.

Decisions or considerations at the rating committee regarding the implications of prevailing credit risk characteristics within a particular sector or country are not key rating assumptions, even where those judgments affect a large number of credit ratings. Moreover, rating committees may consider and decide, from time to time, how to use certain key rating assumptions when assigning a rating, in order to reflect prevailing credit conditions in a certain sector or country (for example to apply higher or lower correlation assumptions, based on the credit risk characteristics of a certain sector or country). Such judgments would not be deemed to change key rating assumptions, since they were not intended to be applied consistently and systematically across most (if not all) debt instruments covered by the relevant methodology.

Macro-economic or financial market projections which are by definition specific to a particular point in time are not key rating assumptions.

For **Structured Finance Credit Rating Methodologies**, key rating assumptions are generally assumptions that underlie the methodology— values assigned to parameters which influence the analysis of a prototypical transaction broadly across the relevant sector. For example:

- Sector correlation assumptions;
- Loss severity expected for the sector;
- Loss rates that serve as a proxy for the collateral performance.

Inputs to the rating of structured finance transactions that result from decisions or considerations by rating committee, or which reflect analytical deliberations, and that are not key rating assumptions, include, for example:

- Rating considerations resulting from credit risk of third parties to the transaction (guarantors, servicers, banks, swap providers). These credit risks are reflected in the credit rating of the third party or the credit estimate.
- Changes in collateral asset risk expectations brought on by changes in the economic environment.

In methodologies relating to **corporate finance and financial institutions**, key rating assumptions are intrinsically rare (because the character of the analysis includes less quantitative parameters) and where they do exist, they may be structurally embedded in the rating methodology. Therefore, notation of key rating assumptions for the subject in the rating methodology is practically meaningless, as change in the key rating assumptions in the rating will usually lead to corresponding change in the rating methodology. Following are examples of embedded key rating assumptions structured into the rating methodology:

- The assumption that leverage and financial flexibility are strong drivers and appropriate factors to include in rating methodologies.
- The assumption of strong interdependence between bank and government credit strength.
- The assumption that legal priority of claim affects average recovery on different classes of debt sufficiently to warrant higher or lower ratings for different classes of debt.
- The assumption that the State of Israel is risk free for the purposes of ratings assigned by Midroog (for example, at ratings of Aaa.il by virtue of government guarantee or if the GRI model is used).

Key rating assumptions that are considered to be distinct from methodology (though they would be listed therein):

- Loss severity in different sectors.
- Default rates when used as a proxy for the state's ability to support the banking system.

Inputs to the rating process that result from judgments or considerations of the rating committee, or reflect analytical deliberations that are not key rating assumptions include, for example:

- The rating considerations arising from credit risk introduced by third parties (guarantors, other support providers, affiliates). These credit risks are reflected in the credit rating of the third party, or credit estimate.
- The government's ability to support the banking system.
- These inputs may include underlying assumptions that do constitute key rating assumptions.

Benchmark parameters used in rating models

Midroog aspires to reflect expected credit losses in an ordinal (relative) scale, i.e., that the expected loss at low ratings will be higher than the expected loss at high ratings, in contrast to measuring specific default and loss rates. Accordingly, ratings are assessments of relative credit risk, not absolute risk assessments.

However, for the purpose of setting a rating for certain financial instruments, Midroog uses models and tools that link between default and loss rates and ratings, in order to use the models' output and tools in the rating process. For that purpose, Midroog relies on default and expected loss rates that Moody's sets. These parameters are defined by rating group and time horizon. By using a set of benchmark parameters, rating models are more likely to provide consistency with respect to the estimation of relative risk across rating levels and investment horizons and can be more easily compared to one another. While Moody's probabilities tables bore some degree of relationship to corporate default and loss experience at the time they were created, that relationship has varied over time, and Moody's continuing use of the Idealized Rates for modeling purposes does not depend on the strength of that relationship over any particular time horizon. The default and loss rates tables, together with other tools and certain assumptions, have a combined influence on the models' output. Also, while absolute

measures are input into the models, the rating performances themselves are tested using measures detailed in the rating performance reports.¹⁵

When we perceive changes in risk that necessitate changes in our credit analysis, this is effected by revision of the data and sometimes in certain assumptions rather than changing the benchmark parameters. This approach enables us to make adjustments that only affect the particular sectors and asset classes we expect will experience significant changes in risk at a given time.

Expected Default and Loss Tables

In the process of determining ratings for certain issuers and financial instruments (such as financial instruments in structured finance and issuers government related issuers), Midroog may use benchmark default and expected loss probabilities. For Idealized default and expected loss probabilities tables see Midroog's website.

The tables can be used in two ways: (1) to suggest benchmark expected default and loss rates for modelling the credit risk of a collateral assets or the risk that a rated- counterparty will fail to perform a role, and (2) to associate different modelled expected loss rates with different benchmark ratings. Please consult Midroog's credit rating methodologies for details.

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¹⁵ For rating performance reports, see Midroog's website.

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