Divestiture of the Credit Card Companies:

Supervisory emphases for interested buyers

Banking Supervision Department, Bank of Israel

As of February 18, 2018

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Sale of control of the companies will take place by January 2020

According to the Promotion of Competition Law, Bank Hapoalim and Bank Leumi are required to sell their holdings in credit card companies Isracard and Leumi Card:

- **Full sale of all the holdings by January 31, 2020**
- If within 3 years from the date the law went into force (January 2017) the banks issue at least 25 percent of the companies to the public and their holdings do not exceed 40 percent of the means of control in the company, the sale obligation will be deferred to January 31, 2021.

Possible paths to a sale

The banks can work in parallel through the following paths:

1. Find a strategic buyer for the company
2. Issue shares and spin off the shares on the stock exchange

   Includes the possible distribution of an in-kind dividend

Basic facts on the companies, as of 9/2017 (NIS million)

	Leumi Card	Isracard	Cal-Israel Credit Cards
Year established	2000	1975	1978
Equity (balance sheet)	1,868	2,678	1,633
Common Equity Tier 1 Capital Ratio	15.70%	19.50%	14.60%
Total assets (balance-sheet total)	14,076	17,778	13,214
Credit to individuals	7,455	4,120	6,168
of which: Interest-bearing credit to individuals	5,404	2,339	3,967
Increase in interest-bearing credit to individuals since 2014	71%	175%	73%
Credit loss allowances (individuals)	1.41%	3.98%	3.91%
Commercial credit	405	1,384	683
of which: Interest-bearing commercial credit (without discounting)	100	1,177	313
Total credit risk that is <u>not</u> guaranteed by banks	7,917	5,504	6,851
Total credit risk guaranteed by banks and others	5,830	11,743	6,062
Number of active cards	2,199	3,317	2,085
of which: Nonbank cards	785	744	703
Number of employees	1,143	1,363	1,330
Efficiency ratio	73.10%	63.48%	66.60%

The credit card companies – strong points

- **Extensive databases on households and businesses**
  - Can enable them to develop and offer additional products of value to customers and to enhance competition in the financial sector overall
- **Considerable and available capital**
- Regulatory knowledge, corporate governance, **experience in risk management**
- **Experience with credit** to households and small businesses
- **Reputation**
- **Innovation** (technology, products, and services)
- **Tailwind by regulator** in promoting the divestiture and competition

The credit card companies – main challenges

- **Separating from the banks** and building some abilities independently
- Constructing **a sustainable business model**
- Diversifying sources of **liquidity/financing**
- **Handling increasing competition** in the credit and acquiring sector
- **Preparing operationally** for the Promotion of Competition Law
- **Marked changes in the payments sector**

Possible purchasers (1)

- The main criteria for granting a control permit include aspects of honesty and integrity, financial robustness, a simple and transparent holding structure, investment strategy, relevant prior business experience, and no conflicts of interest.

Possible purchasers (2)

- **Strategic investors,** such as foreign banks, payment companies, technology entities, and others
- **Israeli financial entities,** with long term assets not exceeding NIS 100 billion
- **Israeli real corporations,** with total annual sales or credit not exceeding NIS 6 billion
- **Financial and real entities from abroad,** with relevant experience
- **Consortium** of above entities
- **Private equity funds** from Israel and abroad

Criteria for Purchasers of Controlling Core

To the extent that the sale is not a complete spinoff of shares on the stock exchange, but through a sale of a controlling core, the purchasers will be:

- Required to hold **a controlling core of at least 30 percent** of the company's capital
- Able **to pledge surplus shares; not more than 10% of controlling core shares**
- **Financing means of control:** The purchasers will be able to raise credit to finance the purchase, though not from the selling bank, and to raise debt through bonds

Regulatory aspects

- The Banking Supervision Department is assisting with the divestiture of the companies and supports their entrenchment as competitive financial entities

Regulatory aspects (2)

- **Interchange fee**
  - A final framework for the interchange fee for the coming years will be published shortly
- **Companies' liquidity/financing sources**
  - **The Banking Supervision Department is working to reduce the need for liquidity** required by companies against bank cards
  - Liquidity sources
    - **Credit lines from banks**: The Banking Supervision Department is working to ease constraints, which will increase the availability of sources and help the credit card companies with the cost of the sources
    - **Bonds from the public**: Under legal restrictions (NIS 2.5-5 billion)
    - Raising sources from **institutional entities**

Regulatory aspects (3)

- **Diversification of activities and sources of income**
  - After the divestiture of the companies, they will not be auxiliary banking corporations **and thus will be able to deal in a wider range of activities**, with the approval of the Supervisor of Banks; alternatively -
- **Receipt of banking license**
  - **Credit card companies will be able to receive a banking license in an accelerated process** and to begin seeking deposits. Regulation of the new bank will be adjusted for size, activities that will be defined, and risks.

Regulatory aspects (4)

- **Digital activities – additional leniencies**
  - During the course of the past year, **leniencies were established for credit card companies**
    - For example: opening a small business account remotely via digital means
    - SOON: Digital account statements – supports increasing efficiency and reducing costs
    - SOON: Expanded outsourcing options
- **Capital requirements:**
  - The **capital adequacy requirements were reduced** relative to large and small banks (Common Equity Tier 1 Capital of 8.5 percent and overall capital adequacy of 11.5 percent)

Regulatory aspects (5)

- Dividend policy
  - **Before the purchase** – The companies that are up for sale are permitted to distribute a dividend and to establish dividend distribution policy on a regular basis with approval of the Banking Supervision Department.
  - **After the purchase** – Dividend distribution policy will be possible in accordance with the strategic plan and risk profiles and with approval of the Banking Supervision Department.

Regulatory aspects (6)

- **Process of examining candidates**
  - The process will last approximately 4 months from the date that all the required documents are submitted to the Banking Supervision Department

- **To contact the Banking Supervision Department:**
  - Ms. Sima Spitzer, Head of the Licensing and New Banks Unit
  - Email: LicensingApplications@boi.org.il
  - Phone: 02-655-2402

Additional details

- **Additional details on the criteria for receiving a permit for control of an acquirer/credit card company and the licensing process, are available on the Bank of Israel website.**