March 30, 2020

# Phoenix shows total earnings of NIS 547 M and 8.6% annualized ROE in 2019

## The Company's favorable results in profit and ROE were achieved despite the significant increase of NIS 1.683 B in insurance reserves for life and LTC insurance, performed due to a decline in interest rates and changes in actuarial assumptions.

The Company's shareholders' equity as of December 31, 2019 was app. NIS 6.5 B, after distribution of a NIS 480 M dividend,[1] with app.

As of December 31, 2019, the Group had AUM in the amount of app. NIS 214 B.

CEO Eyal Ben Simon stated, "The Company's strength, reflected in its results for 2019, creates a solid foundation for the Company's ability to meet the challenges resulting from the Coronavirus pandemic."

Ben Simon noted that the Group has made preparations to provide full protection to the health of its employees and to ensure business continuity and to provide services to its customers and agents. Approximately 3,000 Group employees have been instructed to work full time from home. Ben Simon also noted the Group's preparations to meet the needs of the residents at its Ad 120 retirement homes.

Ben Simon stated, "The Group is also taking several steps in anticipation of the post-crisis period. For example, the Group promoted an agreement on salary cuts between the Company and the labor committee, and performed several steps with employees' needs in mind, including the establishment of several aid funds for the benefit of its employees.. The Company is investing managerial and professional resources to study and deal with the changes in the financial markets, with the recognition that this period offers unique investment opportunities that will allow The Phoenix to bolster its intermediate- and long-term investment portfolio."

According to Ben Simon, the year 2019 once again demonstrated the Company's strengths as owner of diverse and profitable growth engines. P&C, the smart brand, LTS (life insurance, pension and provident funds), health insurance, financial services (Excellence), insurance agencies, credit, and retirement centers.

**Material changes in 2019:**

**Sale of control in The Phoenix** – On November 4, 2019, the Delek Group announced that the conditions (including a control permit issued by the Commissioner of the Capital Market, Insurance, and Savings at the Ministry of Finance) were satisfied for closing the sale of the control nucleus (app. 32.5% of the Company's shareholders' equity) to corporations controlled by Centerbridge Partners LP and Gallatin Point Capital LLC, for the total amount of app. NIS 1.57 B.

**CEO change** – On November 7, 2019, the BODs of the Company and The Phoenix Insurance resolved to appoint Mr. Eyal Ben Simon as permanent CEO of the Company and The Phoenix Insurance.

**Change of CBODs and directors** – After conclusion of the sale of the control nucleus, new directors were appointed by the new controlling shareholders. Mr. Benyamin Gabbay was appointed CBOD of The Phoenix Insurance and temporary CBOD of the Company.

**Dividend distribution** – In April 2019, the Company distributed a dividend of NIS 250 M. On September 18, 2019, the Company distributed all Mehadrin shares in the amount of app. NIS 230 M as a dividend in kind to the Company's shareholders, as part of its reorganization following the Anti-Concentration Law.

[1] Of the distribution, app. NIS 230 M are Mehadrin shares that were distributed as a dividend in kind to Company shareholders to comply with the Anti-Concentration Law.

**Business results 2019:**

**Comprehensive profit attributable to Group shareholders in 2019** totaled app. NIS 547 M, compared to app. NIS 539 M last year.

**Profit for the period attributable to Group shareholders in 2019** totaled app. NIS 155 M, compared to app. NIS 679 M last year.

**Comprehensive loss in Q4/2019 attributable to Group shareholders** totaled app. NIS 32 M, compared to app. NIS 52 M in Q4/2018, mainly due to the low interest environment and as a result of an increase of app. NIS 954 M in insurance liabilities before tax in Q4/2019 due to research conducted by the Company.

**Losses in Q4/2019 attributed to Group shareholders** totaled app. NIS 97 M, compared to profit of app. NIS 97 M in Q4/2018.

The results in 2019 and in Q4/2019 were significantly affected by the downward trend in the yield curve and the illiquidity premium in the local economy, which increased insurance liabilities before tax by app. NIS 1,185 M and by app. NIS 360 M in insurance liabilities before tax, respectively. These effects were in addition to the effects of the Demographic Assumptions Circular in the amount of app. NIS 85 M in 2019. In addition, the effect of changes in actuarial assumptions in the life insurance and health segments led to an increase in insurance liabilities of app. NIS 568 M before tax and app. NIS 594 M before tax, in 2019 and Q4/2019, respectively. This effect was partially offset by a revision to the Company's estimations in the compulsory motor and liability segments following a Supreme Court ruling, which determined 3% as the discount rate used for annuities. Consequently, the provisions in these sectors declined by app. NIS 155 million before tax in 2019.

The total effect is an increase in insurance liabilities in the amount of app. NIS 1,683 M before tax, and app. NIS 954 M before tax in 2019 and Q4/2019, respectively.

In 2018, results were affected by an upward slope in the yield curve and by the effects of changes in actuarial assumptions. The effect of an increase in interest rates and in the illiquidity premium on the decline in insurance liabilities, and the effect of changes in actuarial assumptions, was an increase in profit before tax of app. NIS 55 M in 2019 and a decrease of app. NIS 52 M in Q4/2019.

**P&C** – In 2019, comprehensive profit before tax totaled app. NIS 681 M, compared to app. NIS 269 M in 2018. Comprehensive profit before tax in Q4/2019 totaled app. NIS 157 M, compared to app. NIS 73 M in Q4/2018.

Results in 2019 were materially influenced by a decline of app. NIS 155 M before tax in insurance liabilities in the P&C compulsory and liability segments, as stated above. The increase in comprehensive profit, less the decline in insurance liabilities, stems mainly from a significant increase in investment income and an improvement in underwriting results in the homeowners segment.

**Life insurance and LTS -** In 2019, comprehensive losses before tax totaled app. NIS 276 M, compared to comprehensive profit of app. NIS 273 M in 2018. In Q4/2019, comprehensive losses before tax totaled app. NIS 118 M, compared to app. NIS 129 M in Q4/2018.

**Life insurance -** In 2019, comprehensive losses before tax totaled app. NIS 327 M, compared to profit of app. NIS 219 M in 2018. In Q4/2019, comprehensive losses before tax totaled app. NIS 126 M, compared to app. NIS 135 M in Q4/2018.

The effect of the change in the yield curve and the illiquidity premium led to an increase in insurance liabilities of app. NIS 942 M in 2019, compared to a decline of app. NIS 91 M in 2018, and to an increase in insurance liabilities of app. NIS 395 in Q4/2019 compared to a decline of app. 4 M in Q4/2018.

The effect of the change in the Demographic Assumptions Circular, noted above, led to an increase of app. NIS 85 M recorded in Q2/2019. In addition, the changes in other assumptions used to calculate life insurance reserves led to an increase of app. NIS 59 million in insurance liabilities in 2019, and app. NIS 54 M in Q4/2019, compared to an increase of app. 11 M in insurance liabilities in 2018 and a decline of app. NIS 28 M in insurance liabilities in Q4/2018.

In 2019, variable management fees totaled app. NIS 487 M, compared to 2018, in which no variable management fees were charged. The increase in 2019 compared to 2018 stems from the higher real returns achieved by the Company in 2019 compared to 2018, after the deficit in variable management fees as at December 31, 2018 in the amount of app. NIS 62 M was covered in entirety in Q1/2019. In Q4/2019, variable management fees totaled app. NIS 217 M.

**Pension** – In 2019, profit before tax totaled app. NIS 11 M, compared to app. NIS 28 M in 2018, and totaled app. NIS 2 M in Q4/2019 compared to app. NIS 4 M in Q4/2018.

In 2019, pension benefits contributions totaled app. NIS 4,079 M, compared to app. NIS 3,547 in 2018, reflecting an increase of app. 14.9%. Pension funds AUM as at December 31, 2019, totaled app. NIS 30.7 B, compared to app. NIS 23.7 B as at December 31, 2018, reflecting an increase of app. NIS 29.5%.

**Provident funds** – In 2019, profit before tax totaled app. NIS 40 M, compared to app. NIS 26 in 2018, and totaled app. NIS 6 M in Q4/2019 compared to app. NIS 2 M in Q4.2018. The increase stems mainly from income from management fees, which increased in 2019 due to the increase in AUM, alongside a decrease in management fees as a result of growing competition in the sector, and a decrease in G&A as a result of savings in the Company's operating expenses.

In 2019, contributions to the Group's provident funds totaled app. NIS 2,762 M, compared to app. NIS 2,549 M in 2018, reflecting an increase of 8.4%. Provident funds AUM totaled app. NIS 34.2 B as at December 31, 2019, compared to app. NIS 30.2 B as at December 31, 2018, an increase of app. 13.2%.

**Health** – In 2019, comprehensive losses before tax totaled app. NIS 311 M, compared to profit of app. NIS 79 M in 2018. In Q4/2019, comprehensive losses before tax totaled app. NIS 284 M, compared to app. NIS 30 M in Q4/2018.

Results for the reporting year were materially affected by the downward development in the risk-free yield curve, which increased the LAT reserve in the health (LTC) segment by app. NIS 226 M, compared to a decrease in LAT reserves of app. NIS 96 M in 2018. Results were also adversely affected by revisions to actuarial assumptions as a result of research, which increased insurance liabilities by app. NIS 509 M and NIS 512 M in 2019 and Q4/2019, respectively, compared to an increase in LAT reserves as a result of changes in actuarial assumptions by app. NIS 137 M and app. NIS 114 M in 2018 and Q4/2018, respectively. In 2019, results were favorably influenced by an improvement in investment income compared to 2018.

In 2019, gross premiums totaled NIS 3,257 M, compared to NIS 2,231 M in 2018, reflecting an increase of app. 45.9%, mainly due to the LTC contract with Maccabi, which came into effect from January 1, 2019.

**Financial services -** Comprehensive profit before tax totaled app. NIS 167 M compared to NIS 60 M in 2019 and 2018, respectively. In Q4/2019 and Q4/2018, comprehensive profit before tax totaled app. NIS 38 M and to NIS 18 M. The increase income from financial services stemmed mainly from an increase in ETF management fees compared to 2018, in which the Company recorded losses from these operations. The increase in income also stems from income from a company consolidated for the first time in 2019, and from non-recurring income from reevaluation of the investment in the investee that was consolidated for the first time in Q1/2019 as a result of an increase in control, in the amount of app. NIS 29 M.

**Insurance agencies** – Comprehensive profit before tax totaled app. NIS 171 M and NIS 125 M in 2019 and 2018, respectively. In Q4/2019 and Q4/2018, comprehensive profit before tax totaled app. NIS 46 M and NIS 41 M, respectively. Revenues and comprehensive profit before tax in the agencies sector increased in 2019 and in Q4/2019 mainly due to an increase in sales and the acquisition of additional agencies.

**Solvency ratio of The Phoenix Insurance as at June 30, 2019**

The solvency ratio of The Phoenix Insurance as at June 30, 2019 is 115%. This calculation included capital activities performed from June 30, 2019 to the publication date of the ratio. Excluding these capital activities, and after distribution of a dividend of NIS 621 M in the first half of 2019, the solvency ratio as at June 30, 2019 is 110%.

This ratio does not include the capital activities performed by The Phoenix Insurance in 2019 and up to the approval date of its financial statements for 2019, which include a private placement by an expansion of bonds (Series K) in the amount of app. NIS 800 M, of which app. NIS 601 M were recognized as Tier-2 capital; early redemption of bonds (Series B) in the amount of app. NIS 445 M; and issuance of additional Tier-1 capital in the amount of app. NIS 300 M. These activities, which were performed after June 30, 2019 and up to the publication date of the solvency ratio, increased the solvency ratio to 115%.

In the second half of 2019, the risk-free linked shekel yield curve showed the beginning of a significant downward trend that may adversely affect economic solvency rate of The Phoenix Insurance. Notably, the risk-free linked shekel yield curve rose after the reporting date (December 31, 2019 and up to the publication date of its financial statements for 2019. The more significant rise is on the short end of the curve, with a more moderate rise on the long end. This increase partially offset the effects of declining interest rates in the second half of 2019.

The Company assessed the effects the risk-free linked shekel yield curve on June 30, 2019 results. A decline of 50 base points across the curve would have created a 9% decline in the economic solvency ratio. This result is an estimation based on June 30, 2019 results, and is designed to illustrate the effect of a decline in interest rates on the solvency ratio, and no conclusion should be drawn from this estimation regarding the results, had the calculation been performed on the publication date of the financial statements. The estimation was calculated for a decline of 50 base points across the curve and therefore other changes in the yield curve or changes that are unevenly distributed across the curve would not necessarily have a linear effect on the Company's solvency ratio at that date.

On March 19, 2020, a draft circular was published, amending the Solvency Circular. The aim of the draft circular was to update and adapt the solvency regime in Israel to the European Directive through various means, including an adaptation period between December 3,1 2019 and December 31, 2032, for specific homogeneous classes of insurance reserves in the economic balance sheet. Said amendment may significantly increase solvency ratio of The Phoenix Insurance in the adaptation period.

According to the directives of the Commissioner, the Company is expected to publish its solvency ratio as at December 31, 2019, no later than August 31, 2020.

Activities after December 31, 2019 –

On December 30, 2019, the BOD of The Phoenix Insurance approved a distribution of 100% of the issued and paid-in shares of The Phoenix Excellence Pension and Provident as a dividend in kind to the Company. This distribution is subject to statutory approvals, including approval of the tax authorities and the Capital Market, Insurance, and Savings Authority. As at the publication date of the financial statements, such approvals are pending.

In February 2020, the Company issued CPI-linked bonds (Series 5). Proceeds of the issue, totaling NIS 220 M will be used by the Company to inject Tier-1 capital into The Phoenix Insurance.

**Effects of the Coronavirus**

As at the approval date of the financial statements, the spread of the Coronavirus has a material impact on the Group's operations and results. Prolongation of the Coronavirus crisis and its intensity in Israel may adversely affect the Group's business if the crisis worsens.

At this point in time, the Company's management believes that the most powerful effect is the effect of declines in the financial markets. The Company performed a preliminary estimation for the period beginning after the approval date of the financial statements, regarding the effects of declines in the financial markets in Israel and abroad on the Nostro assets of The Phoenix Insurance. This estimation shows a decline of app. NIS _____ M in tradable Nostro assets before tax. As a result of these declines in customers' portfolios, variable management fees of app. NIS ____ M will not be charged in the future. In contrast, the rise in the risk-free yield curve, which occurred in this period, is expected to reduce the insurance reserves.

**The Company has taken and continues to take action to adjust the Group's expenses to the anticipated decline in revenues:**

1. **Variable costs** – Due to the nature of the Group's operations, one third of the decline in revenues is automatically offset by a decline in its direct expenses, such as distribution commissions, operating costs, and other expenses that are a function of the volume of its assets.

2. **Fixed costs** – Reduction in expenses that are not a function of the volume of its assets.

3. **Payroll expenses** – The Phoenix Insurance reached an agreement with the labor committee, based on the following main points:

(a) Across the board cut in wages of employees and managers beginning from May 2020, of between 7% and 10%. No wage cut will be applied to employees who wages are NIS 7,000 or below.
(b) Cancellation of the salary hikes for the years 2019-2021 that were defined in the collective labor agreement.
(c) Advance payment of 3.4% on average, at the expense of the salary hike to be defined in the future collective labor agreement.
(d) Employees on leave will continue to receive social benefits until end April 2020.
(e) The Phoenix Insurance will pay a special one-time bonus for 2019 equal to 30% of the wages, which will be paid together with employees' March 2020 salary. A money fund will be established to provide financial assistance to employees, and a fund will be established for reimbursing vacation days to employees who entered into a deficit of vacation days due to their leave.

This estimation is based on the trends that are known at the today, and as the duration and scale of the spread of the Coronavirus increase, additional significant effects on the Group's results may occur, including an exacerbation of the existing effects, such as: a change in the value of investment assets, a decline in returns for policyholders and in the management funds that are a function of these returns, and an increase in lapses and withdrawals of insurance policies. The Company's ability to raise debt and capital in the future may also be adversely affected.

These estimations may not materialize, in part or in entirety, or may materialize in a manner that differs materially from these estimations. The Group continues to monitor the developments in Israel and abroad continuously and will continue to provide updates as necessary of material implications of the spread of the Coronavirus on the Group's operations, if any.

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