2023

THE

ANNUAL REPORT

Government Debt Management Unit
Accountant General's Office
Ministry Of Finance

החשב הכללי
Accountant General

TABLE OF CONTENTS

Remarks of the Accountant General

Executive Summary

Government Debt Management Objectives 6
Issuance Strategy 6
Debt-to-GDP Ratio 6
Issuance in 2023 7
Government Debt Portfolio 7
Government Debt Interest Expenditures 8
Israel's Credit Rating 8
Government Debt Average Time to Maturity 9
Non-Tradable Domestic Debt 9
External Debt 9
Tradable Domsetic Debt 9
Trading of Government Bonds on the Secondary Market 10

Macro-Economic and Market Review

Market Summary and Macro-Economic Impact on Debt Management 12
Israel 12
Global Economy 13
Global Markets 13
Debt Management 15

Primary Market

Local Issuances 18
Tradable Domestic Debt 18
Issuing Tools 19
Short-Term Bonds 21
Tradable Securities Issued on the Domestic Market in 2023 21
Coverage Ratio 22
New Series in the Domestic Market 22

Global Markets 23
Sovereign Issuances 23
The State of Israel's First Green Issuance - January 2023 24
Global Public Offerings - March 2024 24
Private Placements 24
Issuances through the Israel Bonds Organization .. 25
United States Government Guarantees 26
Loans from Foreign Governments and Other Loans...26
The State of Israel's Credit Rating 27
Development of Israel's Credit Rating 27
Yields on Foreign Currency Denominated Bonds Issued by the Israeli Government 28

Debt Portfolio

Government Debt 36
Debt-to-GDP Ratio 37
Interest Expenses 38
Government Debt Risk Management 39
Average Issuance Amount and Number of Series 43

Non-Tradable Domestic Debt

Non-Tradable Domestic Debt in 2023 46
The subsidy cost of the Non-Tradable Debt 48

Organizational Chart



Remarks of the Accountant General

It is an honor to present the 2023 Annual Report prepared by the Government Debt Management Unit of the Accountant General's Office. The annual report is an important element in increasing transparency of government debt management. It includes an analysis of the domestic and international debt profiles, risk management metrics and the capital raising strategy, while analyzing the impact of the war on the government debt.

The year 2023 was challenging for the Israeli economy, as it dealt with complex external and internal challenges, which caused an increase in economic uncertainty, with the most significant event being the "Iron Swords" war following the murderous terror attack on October 7, 2023. This was preceded by the government's proposed legislative changes to the judicial system, and the extensive public protest that followed. The war, which substantially changed the economic outlook of 2023, brought about far-reaching consequence which were reflected in changes to government offices' priorities, a substantial increase in expenditures and a decrease in revenue, triggering a sharp rise in financing needs.

The State of Israel entered the war with a very strong debt profile. The average time to maturity (ATM) of the debt portfolio stood at more than 9 years, the debt Rollover Ratio amounted to approximately 8%, and the debt-to-GDP ratio was only roughly 60%. Had it not been for the war, the downward trend of the debt-to-GDP ratio was expected to continue. As anticipated, the debt-to-GDP ratio for 2023 rose to roughly 61.9%, due to increased military and civilian expenditures and support of the economic activity, and we expect this trend to continue in 2024. The downward trend of the debt-to-GDP ratio and the responsible government debt management throughout the years, are what enabled the government to operate with the financial flexibility required to finance its activities and undertake fiscal expansions in times of emergency and crisis.

Due to the sharp increase in the State of Israel's financing needs stemming from the outbreak of the war, the amount of capital raised over the fourth quarter of 2023 substantially increased. Debt was raised both on the tradable domestic market and across international markets, reaching a total of roughly NIS 160 billion for 2023, about NIS 81 billion of which was raised following the start of the war. Despite the sharp increase in the amount issued, the average coverage ratio (surplus of demand relative to supply) of domestic capital market issuances reached about 4.7, compared to the average coverage ratio of 4.3 in the first three quarters of 2023. The ability to respond quickly to the increase in financing needs was possible thanks to broad access to domestic and international capital markets, a diverse international investor base, as well as the Israel Bonds organization as an active investor.

Against the backdrop of the many economic challenges, 2023 saw extensive professional, public, and media interest in the credit rating of the State of Israel. In November 2023, following the outbreak of the war, the credit rating agency S&P reaffirmed the rating of the State of Israel at AA- and updated its outlook from "Stable" to "Negative". In October 2023, the credit rating agency Fitch reaffirmed Israel's credit rating at A+ but placed Israel on "Negative Rate Watch" due to the possible market impacts of the war. In April 2024 the credit rating agency Fitch removed Israel from Rating Watch Negative, and changed Israel's rating outlook from "Stable" to "Negative". In April 2023, the rating agency Moody's reaffirmed Israel's credit rating at A1 but changed its rating outlook from "Positive" to "Stable". In November 2023, Moody's placed Israel on "Negative Rate Watch". In February 2024, for the first time since Israel first received a credit rating, the rating agency Moody's downgraded Israel's credit rating to A2, with a "Negative" outlook.

In March 2024, for the first time since the outbreak of the war, Israel issued dollar-denominated bonds through public offerings on international markets. Three new bonds were issued, having 5-year, 10-year, and 30-year maturities totaling USD 8 billion. The issuance received the highest demand in the history of the State of Israel, reaching a peak demand book of USD 38 billion. Participating in the issuance were over 400 high-quality strategic investors from about 36 different countries. The selected issuance method in which bonds are issued with three different maturities along the yield curve, provides access to a broad and diverse investor base, decreases financing costs, and is aligned with common practices among many countries. The success of these bond offerings reflects an unprecedented indication of confidence in the Israeli economy by the world's largest international investors. This confidence has been built over many years and enables the diversification and deepening of the financing channels of the government debt. The capacity to raise capital in the foreign markets, including during a war, in very substantial amounts, and at high coverage ratios, demonstrates Israel's extensive access to markets and the resilience of the Israeli economy.

In conclusion, I wish to thank the staff of the Government Debt Management Unit under the Financing Division for their extensive efforts and for their effective and high-quality management of the debt in a challenging period and an economically complex environment, while providing swift and effective solutions to the changing financial needs.

Well done.

Respectfully,

Yali Rothenberg
Accountant General, Israel Ministry of Finance

EXECUTIVE SUMMARY

WE ARE PLEASED TO SUBMIT THE ANNUAL REPORT FOR 2023 ON BEHALF OF THE GOVERNMENT DEBT MANAGEMENT UNIT OF THE ACCOUNTANT GENERAL (THE "GDMU").

Government Debt Management Objectives

The mission of the GDMU is to finance government activities while serving the long-term strategic objectives of government debt management for the State of Israel (the "State"). This policy addresses the State's considerations as an issuer by balancing the cost of issuing debt with exposure to risk. It also addresses the State's considerations as a sovereign by supporting and developing the Israeli capital market, especially the government bond market.

The volume of debt funding directly impacts the debt-to-GDP ratio, as well as the interest burden on the state budget, in the form of ongoing interest payments. Pre-planned issuances are based on financing needs derived from the expected deficit and in line with the cash flow requirements of refinancing existing debt. Funding channels, maturities, and composition of issuances are determined according an annual and multi-year strategic plan, with necessary adjustments made as needed in response to ongoing financial market developments and the financing needs of the State.

Issuance Strategy

The strategy for raising debt is determined based on a wide range of models, indicators, and simulations aimed at minimizing financing costs within a desired threshold of risk. The issuance strategy is based on qualitative considerations, observable implications from the structure of government bond curves, increasing liquidity, development and deepening of bond markets, broadening the investor base, and more. This issuance strategy is implemented through three main channels of debt issuance:

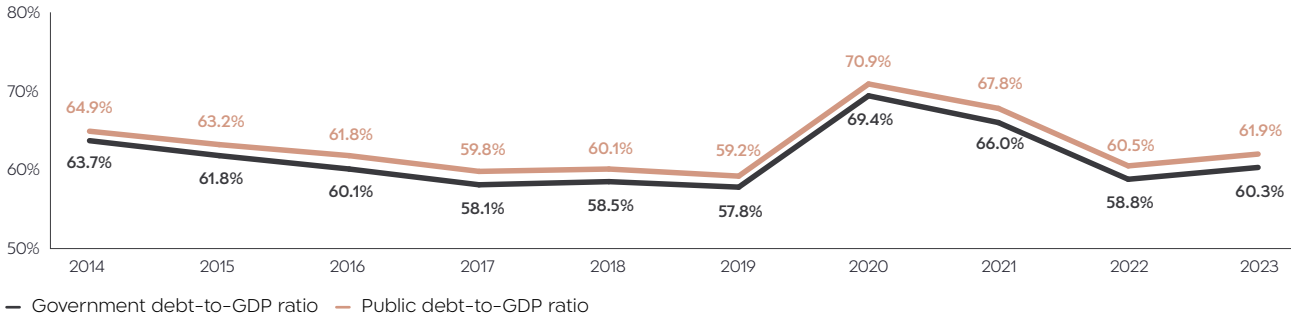
1	2	3
Issuance of Tradable Domestic Debt	Issuance of Non-Tradable Domestic Debt	Issuance of Foreign Debt

Debt-to-GDP Ratio

The debt-to-GDP ratio is a key indicator for evaluating the State of Israel's financial strength. In the years leading up to the COVID-19 pandemic, the State's debt-to-GDP ratio had consistently trended downward, which was notably positive compared to global trends. According to the Accountant General's projections, this downward trend was expected to continue in 2023. However, the outbreak of the "Iron Swords" war led to a sharp and swift increase in government financing needs. Net government debt issued from October to December amounted to roughly NIS 50 billion, out of the net debt issued for all of 2023, totaling approximately NIS 55 billion.

The public debt-to-GDP ratio in 2023 increased by roughly 1.4% compared to 2022, reaching 61.9%. The government debt-to GDP-ratio in 2023 increased by about 1.5% compared to 2022, reaching roughly 60.3%.

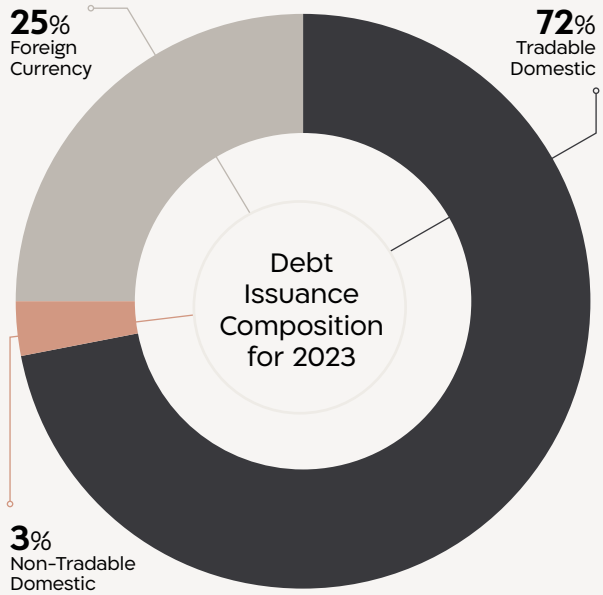
Government and Public Debt-to-GDP



Issuance in 2023

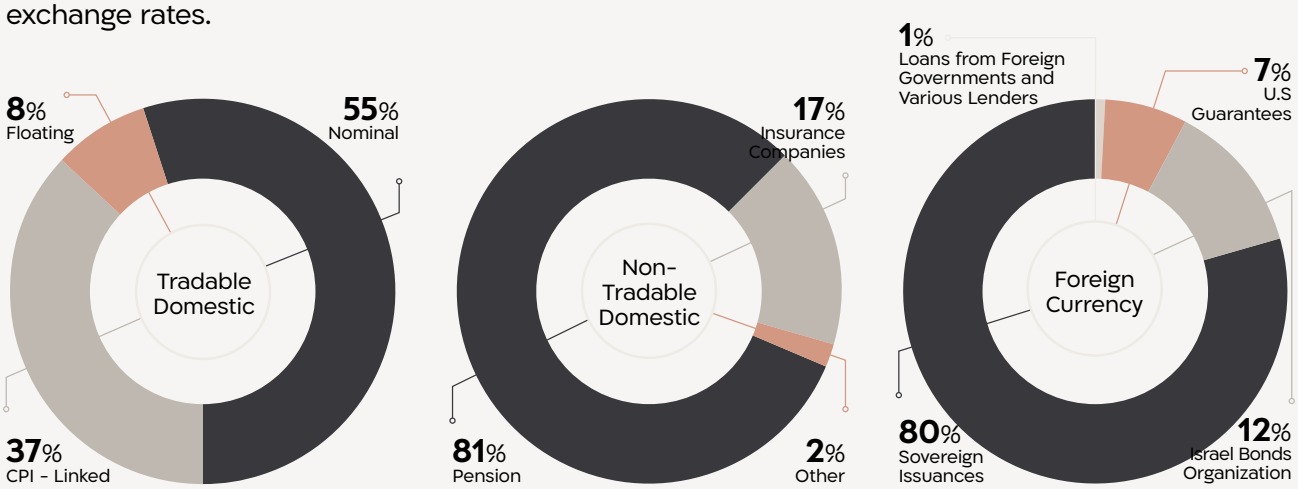
In 2023, the gross debt raised by the GDMU was approximately NIS 160 billion, of which roughly NIS 81 billion was raised following the outbreak of the "Iron Swords" war. for comparison, about NIS 63 billion was raised in 2022.

In 2023, issuance in the domestic tradable channel amounted to an estimated NIS 116 billion. Roughly NIS 5 billion in debt was raised in the domestic non-tradable channel, and an estimated NIS 40 billion was raised in foreign markets.



Government Debt Portfolio

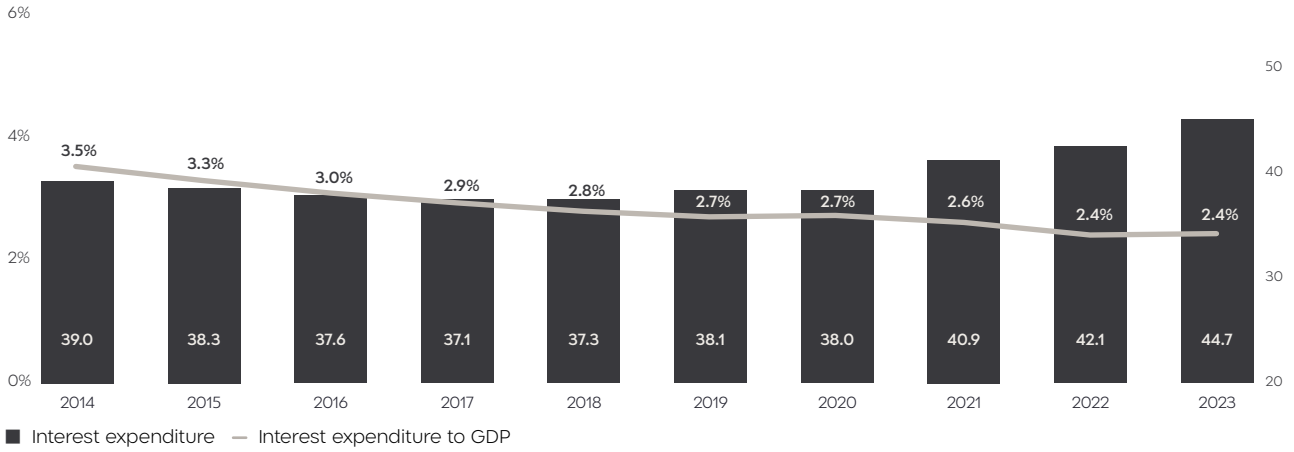
In 2023, government debt increased by approximately 8.7% and stood at about NIS 1,127 billion compared to roughly NIS 1,037 billion in 2022. The nominal increase in government debt is primarily due to the net positive NIS 55 billion of debt raised. The increase in government debt of roughly NIS 35 billion was also influenced by market factors such as inflation, interest rates, and currency exchange rates.



Government Debt Interest Expenditures

The rate of interest expenditure to GDP in 2023 was 2.4%, similar to 2022, continuing the downward trend observed over the last decade. Total nominal interest expenses increased over the years due to the nominal increase in total debt, the increase in the consumer price index (which impacts CPI-linked bonds), and the general rise in government bond yields paid in Israel and abroad. Nevertheless, the rate of interest expenditure to GDP continued to decline, reflecting the greater relative increase in GDP.

Interest Expense to GDP 2014-2023 (NIS billions, Percent)



Israel's Credit Rating

Following the outbreak of the "Iron Swords" war, the credit rating agencies made adjustments to Israel's rating profile.

In November 2023, S&P reaffirmed Israel's credit rating at AA- and updated the outlook from "stable" to "negative".

In April 2023, Moody's reaffirmed Israel's credit rating at A1 and updated the outlook from "positive" to "stable". In October 2023, it placed Israel's credit rating on a "rating watch negative". In February 2024, Moody's downgraded Israel's credit rating by one level, to A2, and updated its outlook to "negative". This concluded Moody's "rating watch negative" rating examination.

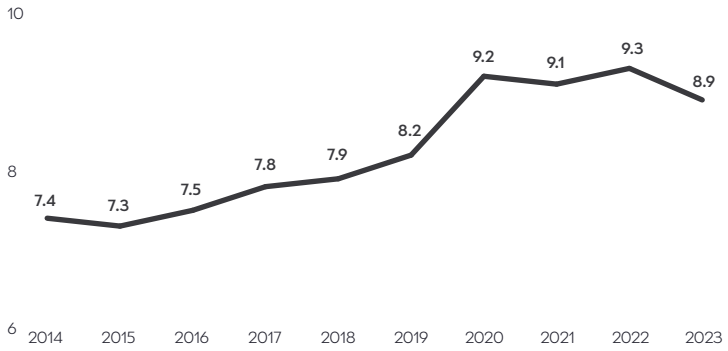
In October 2023, Fitch Ratings left Israel's credit rating at A+ but placed it under "Rating Watch Negative". In April 2024 Fitch removed Israel from "Rating Watch Negative", and changed Israel's rating outlook from "Stable" to "Negative".

Credit Rating Agency	Foreign Credit Ratings	Outlook
Moody's	A2	Negative
Standard & Poor's	AA-	Negative
Fitch	A+	Negative

Government Debt Average Time to Maturity

In 2023, the average time to maturity ("ATM") of the government debt (domestic tradable, domestic non-tradable, and external) decreased to 8.9 years, compared to 9.3 years in 2022. The decline in ATM is attributable to the outbreak of the "Iron Swords" war and the sharp increase in financing needs. In this context, substantial debt with 3 to 10-year maturities was issued from October 2023 onwards.

Government Debt ATM, 2014-2023 (Years)



Additional information about the risk associated with government debt is provided in the Debt Portfolio chapter.

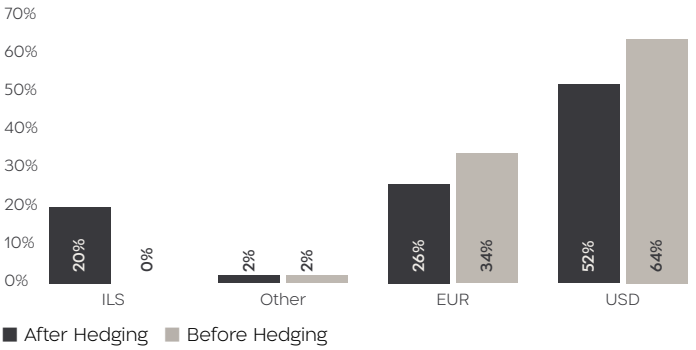
Non-Tradable Domestic Debt

In 2023, non-tradable domestic debt constituted about 30% of the debt portfolio. It was the first year in which no "Arad" designated bonds were issued to pension funds after the reform canceling designated bonds took effect in October 2022. The proportion of non-tradable debt out of all issued debt had substantially decreased from an average of roughly 20% in recent years to approximately 3% in 2023. Debt raised through domestic non-tradable debt channels in 2023 amounted to roughly NIS 5 billion, compared to about NIS 12 billion in 2022. Most of the issuance is attributed to refinancing of debt issued to insurance companies.

External Debt

In 2023, the debt raised in foreign currency-denominated issuances amounted to roughly 16% of the entire debt portfolio. During the last quarter, following the outbreak of the "Iron Swords" war, 14 private issuances were carried out in foreign currencies totaling roughly NIS 23 billion.

Exposure to Foreign Currencies by Currency Without and With Hedging Transactions



In March 2023, a public issuance of USD 8 billion in the global markets was completed, for the first time since the start of the war. The issuance consisted of three tranches: 5-, 10-, and 30-year maturities. Demand in the issuance peaked at USD 38 billion (4.75x the amount raised) - the highest ever for Israel.

To manage currency exchange risk, the GDMU conducts hedging transactions in accordance with an organized hedging plan. As of the end of 2023, without accounting for hedging, roughly 64% of the external debt portfolio was US Dollar-denominated, roughly 34% of the portfolio was Euro-denominated, and the remaining 2% was denominated in other currencies. After accounting for executed hedging transactions, the exposure of external debt to US Dollar, Euro, and other currencies falls to levels of 52%, 26%, and 2%, respectively.

As a result of the hedging transactions, roughly 20% of the external debt portfolio is, in effect, tied to the Shekel.

Tradable Domsetic Debt

In 2023, the government's shekel-denominated tradable debt amounted to roughly 54% of the total debt portfolio, compared to 53% in 2022. Furthermore, the debt raised in 2023 in the tradable domestic channel amounted to 72%, compared to 65% in 2022, among other things, as a result of the "Arad" bond reform taking effect, with "Arad" bonds ceasing to be issued as of October 2022. Debt raised in 2023 in the tradable domestic market amounted to roughly NIS 116 billion, of which about NIS 36 billion was issued via tender offerings in the final quarter, and about NIS 16 billion was issued via swap offerings.

Trading of Government Bonds on the Secondary Market

Trading in government bonds during 2023 was volatile throughout the year, with trading volumes increasing across all channels compared to the previous year. Yield curves traded in 2023 reflect a mixed trend, with decreased short-and medium-range yields alongside increased long-range yields. The yield for the 10-year maturity government bond of the State of Israel as of the end of 2023 amounted to 4.09%, compared to 3.56% at the end of 2022.

In 2023, the State of Israel faced economic challenges marked by an increase in uncertainty, primarily due to the terror attack on October 7, which led to the "Iron Swords" war. The challenges brought on by the war led to a sharp increase in financing needs, requiring an immediate response in order to enable maintaining of the government's capital raising capability and financing of the government activities.

Government capital raising has been continuous, requiring adjustments to changing market conditions while focusing on three central objectives: effective management of the Treasury, supporting the needs of the domestic bond market, and mitigating costs of debt portfolio management, all while considering the multi-year strategy for government debt management. Despite the significant increase in financing needs during a period of uncertainty, the Government Debt Management Unit maintained access to domestic and international markets and expanded the government capital raised as needed, reaching roughly NIS 160 billion.

In March 2024, for the first time since the outbreak of the "Iron Swords" war, Israel issued dollar-denominated bonds on international markets. The issuance totaled USD 8 billion with three maturities of 5, 10, and 30 years. Market demand reached approximately USD 38 billion - the highest recorded in Israel's history.

The substantial demand for tradable bond offerings observed both in Israel and across global markets, despite heightened uncertainty and increasing financing needs, underscores Israel's capacity to raise substantial capital through the domestic and international markets, including in complex time periods. This reflects investor confidence in Israel and its broad access to capital markets.

We wish to thank all of the staff at the Government Debt Management Unit for their high-quality and dedicated work, fulfilling the important task of financing the government's needs, and for their ability to respond to any challenge, even during complex and challenging times.

We hope you find this report informative and insightful.

Respectfully,

Gil Cohen

Senior Deputy Accountant General

Head of Finance, Debt and Credit Division

Philip Yhelzon

Head of the Government Debt Unit

2 MACRO-ECONOMIC AND MARKET REVIEW

MARKET SUMMARY AND MACRO-ECONOMIC IMPACT ON DEBT MANAGEMENT

Israel

In 2023, increased uncertainty characterized the Israeli economic environment, which mainly stem from local motives. The year began with a lack of certainty regarding Israeli markets. In the fourth quarter of the year, the "Iron Swords" war began - which had a significant impact on uncertainty across Israeli capital markets.

As of end of the third quarter, economic growth amounted to 2.7% (annual rate), and the economic was characterized with a tight labor market with low rates of unemployment and a decreased debt-to-GDP ratio. Inflation in Israel was slowing down and converging towards the Bank of Israel's desired target range of 1%-3%. The beginning of the "Iron Swords" war on October 7 drastically altered the existing picture of the Israeli economy - many civilians were evacuated from their homes, many were drafted for reserve duty, the education system was suspended for several weeks and the home front had limited operations while putting many employees on unpaid leaves of absence. Altogether, these factors substantially influenced consumer spending, and public spending, the latter facing a sharp increase due to higher security and civilian costs.

As the war's outbreak ignited increased economic uncertainty, the Bank of Israel stated that, before the next day of trading, it could potentially sell up to USD 30 billion. The purpose of this plan was to mitigate the exchange rate volatility of the shekel and to provide market liquidity for ongoing activities. Within this framework, the Bank of Israel sold USD 8.2 billion in October and roughly USD 338 million in November 2023. In November, The shekel was strengthened, ending stronger than pre-war levels, at 3.63 shekels per US dollar.

Following the increased uncertainty in Israel, and after the outbreak of the Iron Swords war. The rating agency S&P Global Ratings updated. Its rating outlook from "Stable" to "Negative". The rating agency Moody's Investor Services which downgraded its outlook from 'Positive' to 'Stable' in April 2023, placed its outlook on a negative rating review. In February 2024, Moody's downgraded Israel's credit rating by one notch, to A2 from A1, with a "Negative" outlook. The rating agency Fitch which stated in October 2023 that the credit rating of Israel was on "Rating Watch Negative", removed Israel from "Rating Watch Negative" in April 2024, and changed Israel's credit outlook from "stable" to "Negative".

Bank Of Israel's tightened monetary policy adopted in April 2022 continued in 2023. Consequently, inflation throughout the year converged towards the rate in December 2023, reaching an annual rate of 3% - the upper limit of the Bank of Israel's desired target range. During 2023, the Monetary Committee of the Bank of Israel raised interest rates by 1.5%, over four increases. In 2022, the Bank increased rates in seven consecutive meetings. Overall, interest rates have increased, within the current cycle of interest rate hikes, from 0.1% to 4.75%. Starting in May 2023 and continuing through to the end of the year, the Bank of Israel kept interests rates unchanged at 4.75%. In January 2024, in accordance with the ongoing war and the continued convergence towards the inflation target range, the Bank of Israel lowered rates for the first time since June 2020, by 0.25%. As of February 2024, the Bank of Israel's interest rate stands at 4.5%.

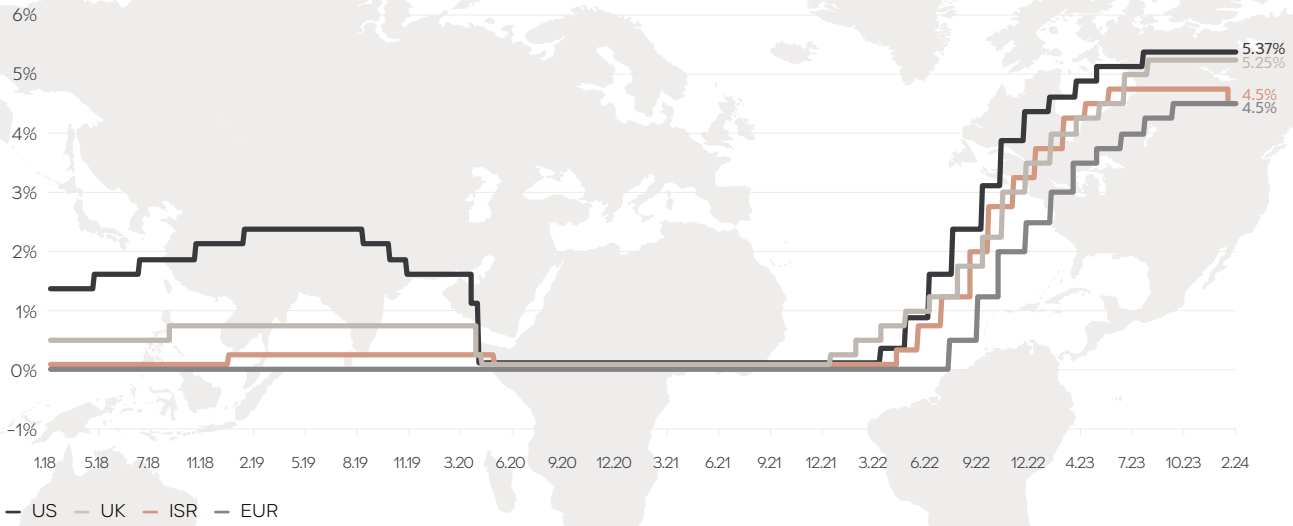
On the fiscal side, in 2023 the budget deficit was approximately NIS 77.5 billion, reflecting roughly 4.2% of GDP, compared to the target deficit rate of 3.7%. The increase in the budget deficit primarily occurred in the fourth quarter of 2023 following the war and by the increase in security and civilian expenditure, alongside the decrease of the State's revenues as a consequence of the war.

Global Economy

During 2023, the world's central banks was continued with the tightening monetary policy which conducted in 2022, in response to the increased inflation. There were also concerns that raising interest rates would harm economic activity or possibly lead to a recession. The US Federal Reserve (the "Fed") raised rates from 0-0.25% at the start of 2022, reaching 5.25%-5.50% by the end of 2023. In 2023, itself, rates increased from 4.25%-4.50%. The European Central Bank (the "ECB") increased interest rates from 0% at the begining of 2022 to 2.5% by the end of the year. In 2023, the ECB continued to lift rates, reaching 4.5% by the end of the year.

Increased interest rates around the world led to a sharp decrease in inflation in many countries. This followed the trend set in 2022 when inflation reached a high of over 9% in the US, EU, and UK. As of December 2023, the annual inflation rate in these countries were 3.4%, 2.9%, and 4%, respectively. In Israel, inflation fell to an annual rate of 3% in December 2023, following a peak of roughly 5.3%, the highest since 2008.

The interest rate of central banks



Global Markets

In 2023, major stock markets worldwide experienced a correction. Following sharp declines in stock prices amid high interest rates in 2022, the year 2023 saw significant gains on leading indices. The S&P 500 index, for example, increased by roughly 24% in 2023; the NASDAQ closed the year with gains of about 43%, and in Europe, the Euro Stoxx index increased by about 17%.

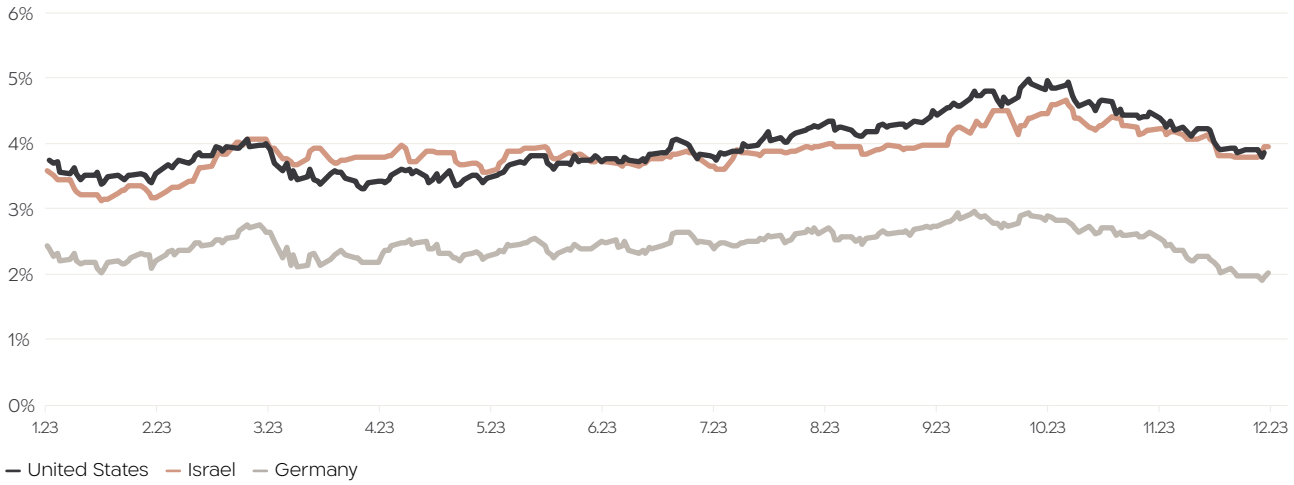
In Israel, after years of strong domestic stock market gains, capital market yields were subpar relative to corresponding indices in the US and Europe. The outbreak of the Iron Swords war on October 7 led to sharp declines of stock price. From then and throughout October, the value of the main indices decreased by roughly 12% on average. By the end of 2023, market uncertainty was eased, and prices began to increase. At the end of the year, the main stock indices in Israel rose by roughly 4% on average.

Government bond yields increased worldwide in 2023, continuing the sharp upward trend that began in 2022 due to rising interest rates. Towards the fourth quarter of the year, yields began to decline in response to decreasing inflation rates and market expectations for the end of the interest rate hike cycle and the worldwide. In the US, 10-year government bonds yields were roughly 3.88% at the start of the 2023 and remained around the same level by the end of the year, following a peak

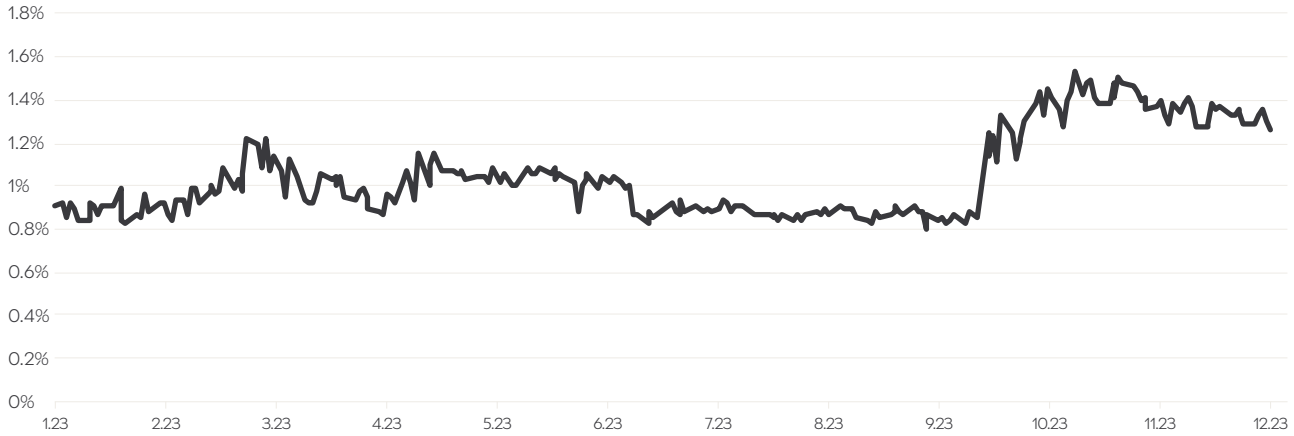
rate of around 4.99%. In Germany, 10-year government bonds traded at 2.43% at the beginning of 2023, reached a high of 2.96%, and closed the year at 2.02%.

In Israel, 10 years government bond yields increased throughout 2023, reaching a peak of 4.655% at the end of October. From November to the end of the year, yields trended downward, and at the close of 2023, the bonds yielded roughly 3.95% (compared to 3.59% at the beginning of the year). USD-denominated 10-year government bonds saw an increase in spreads compared to corresponding bonds in the US during the final quarter of 2023, reflecting heightened risk since the outbreak of the war. At the end of 2023, the spread between bonds was 130 basis points, compared to 90 basis points at the start of the year.

10-years government bonds yields



Israel USD 10-years government bond and US 10-years Government bond spread



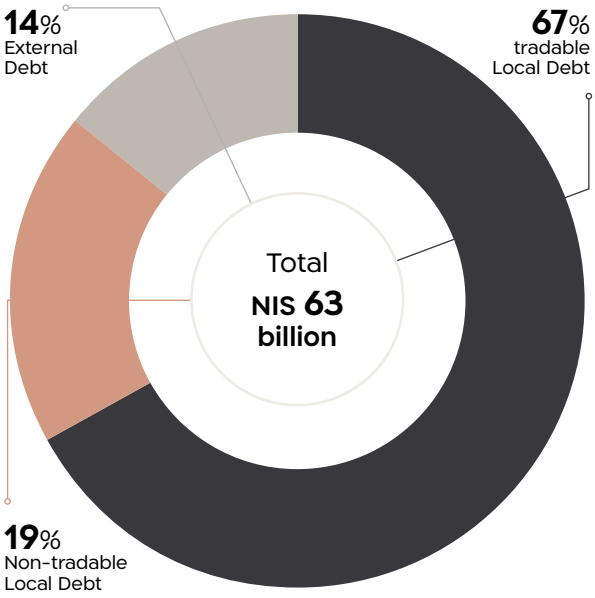
Debt Management

In 2023, financing needs rose, primarily during the final quarter, due to the outbreak and consequences following the start of the "Iron Swords" war. Total domestic issuances of government bonds, including switch auctions, amounted to roughly NIS 116 billion, compared to NIS 42 billion in 2022.

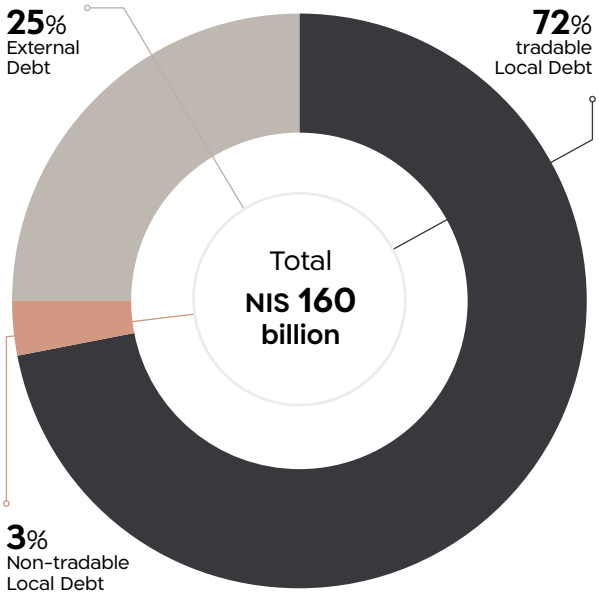
There was a sharp decrease in domestic non-tradable market issuances, attributable to the designated bonds reform that came into effect in October 2022. The total capital raised in 2023 through this channel totaled NIS 5 billion, compared to NIS 12 billion in 2022.

In the external channel, NIS 40 billion was raised through public and private global debt issuances and via the Israel Bonds Organization, compared to roughly NIS 10 billion in 2022.

2022



2023





PRIMARY MARKET



3

LOCAL ISSUANCES

Tradable Domestic Debt

Tradable domestic issuance is the state's prime funding channel. As an issuer, this channel offers the State convenient and continuous access to the capital market, even under conditions of uncertainty and dynamic financing needs. Additionally, this channel has strategic importance to the State as sovereign, as it builts a foundation for financial markets, corporate financial instruments, loans, mortgages, derivatives and more.

CAPITAL RAISED THROUGH THE DOMESTIC TRADABLE CHANNEL IN 2023 AMOUNTED TO ROUGHLY NIS **605.9** BILLION, COMPARED TO NIS **550.5** BILLION IN 2022.

The Government Debt Management Unit ("GDMU")'s domestic tradable debt strategy relies on three primary channels: shekel-denominated, CPI-linked, and floating-rate. Most issuances in 2023 were shekel-denominated (including short-term bonds with maturities of less than one year) and comprised roughly 67% of the capital raised, compared to 27% raised through CPI-linked debt and 6% raised in the floating-rate channel.

Capital was raised in this manner under debt management policy and the objectives of creating a liquid shekel curve and mitigating the general exposure of the public debt and interest payments to changes in the consumer price index.

Primary Channels for Domestic Tradable Capital Financing:

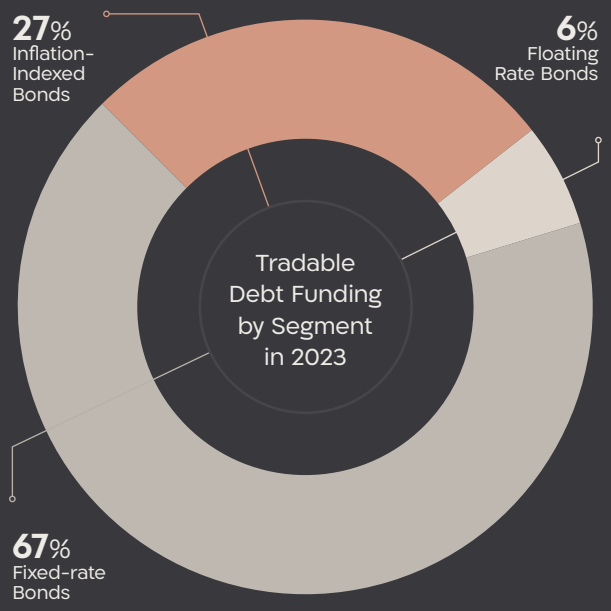
Focus on Shekel-Denominated Issuances - Issuances of domestically tradable instruments are primarily shekel-denominated due to the high exposure of the debt portfolio to the consumer price index (because of tradable debt instruments and "Arad" bonds). At the close of 2023, the amount of CPI-linked debt totaled roughly NIS 222.6 billion, constituting approximately 37% of the public debt.

Support for the Inflation-Linked Curve - The GDMU issues tradable CPI-linked bonds in the domestic market as part of its policy to diversify financial resources and meet existing market demand for these instruments. Since October 2022, CPI-linked Arad bonds ceased to be offered as a result of the "Ensuring Yield" reform (further details about this topic can be found in the Non-Tradable Funding chapter of the 2022 Annual Report).

Floating-Rate Bonds - The GDMU issues tradable floating-rate bonds in the domestic market with consideration of financing costs, distribution of risk, diversifying financing resources, and increasing the flexibility in debt management.

Fundraising Policy:

The capital-raising policy for 2023 relied on the strategic plan for public debt management and utilized different financing channels, with adjustments as needed, aiming to adequately support the market and address the changing financing needs of the government. Similar to previous years, the most capital was raised through issuing tradable bonds on the domestic market, amounting to roughly NIS 116.06 billion, compared to NIS 41.5 billion and NIS 119 billion for the years 2022 and 2021, respectively. Net capital raised on the domestic market totaled roughly NIS 35.8 billion compared to the negative net capital of NIS 46.5 billion in 2022.



The timing of issuances and the amounts raised throughout the year are determined based on the monthly deficit and cash flow of the State. Following increased financing needs in the fourth quarter due to the "Iron Swords" war, the average time to maturity slightly decreased in 2023 to 9.1 years, compared to the average of 9.2 years for the ten years prior to 2023.

Issuing Tools

Funding is executed via weekly auctions and other tools with the purpose of implementing the long-term strategy and dynamically managing government liquidity.

Below are the Primary tools Utilized in addition to Weekly Tender Offerings:

→ Switch Auctions

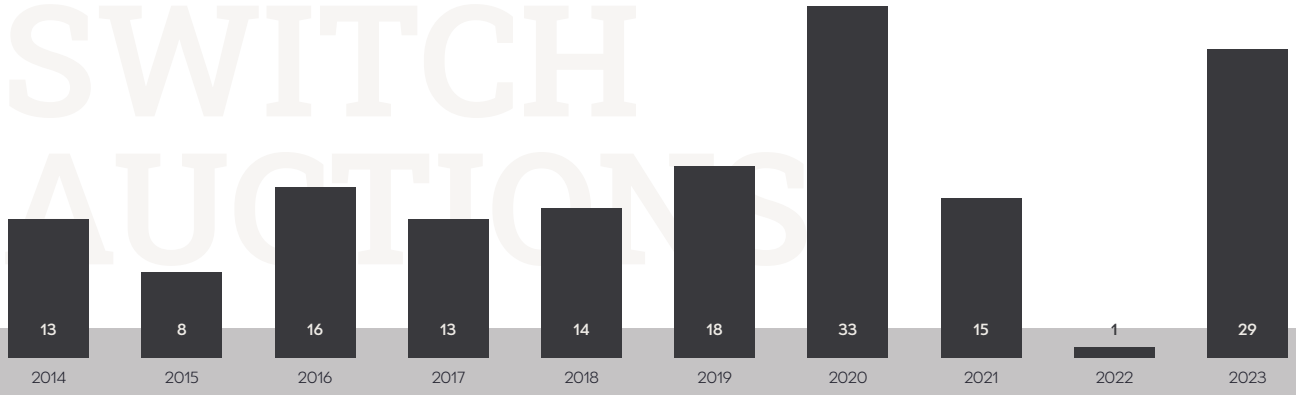
In switch auctions, short-term (less than one year) tradable securities are exchanged for those with longer maturities, both of which are not issued regulary as part of the issuance composition (Off-The-Run). These auctions help stabilize the repayment curve, manage cash flows efficiently, minimize refinancing risk, extend the average time to maturity, increase flexibility in debt management, and enable to implement tactical adjustments in response to real-time changes in the financial markets. Factors considered when selecting Off-the-Run securities for exchange through this method include addressing market demand, increasing liquidity, supporting smaller series, and correcting anomalies in the secondary market.

Additionally, the GDMU utilizes switch auctions to increase the liquidity of new issuances by exchanging Off-the-Run securities for new benchmark On-the-Run securities.

Switch tenders are carried out using the cash neutral method, in which the nominal value of the issued bond and the purchased bond is the same. This allows debt refinancing to be carried out without using funds. Switch tenders are also used as a tool for managing the government's cash flow, as they enable early redemptions and allow issuances to be spread out over the course of the fiscal year, as well as between years.

In 2023, following a significant rise in financing needs, more capital was raised through switch auctions, amounting to roughly NIS 29.4 billion, compared to about NIS 1.3 billion in 2022. Over the past three years, an average of roughly 17% of all domestic tradable securities were issued through this mechanism.

The graph below illustrates switch auctions sizes over the past decade:



→ Buyback Auctions

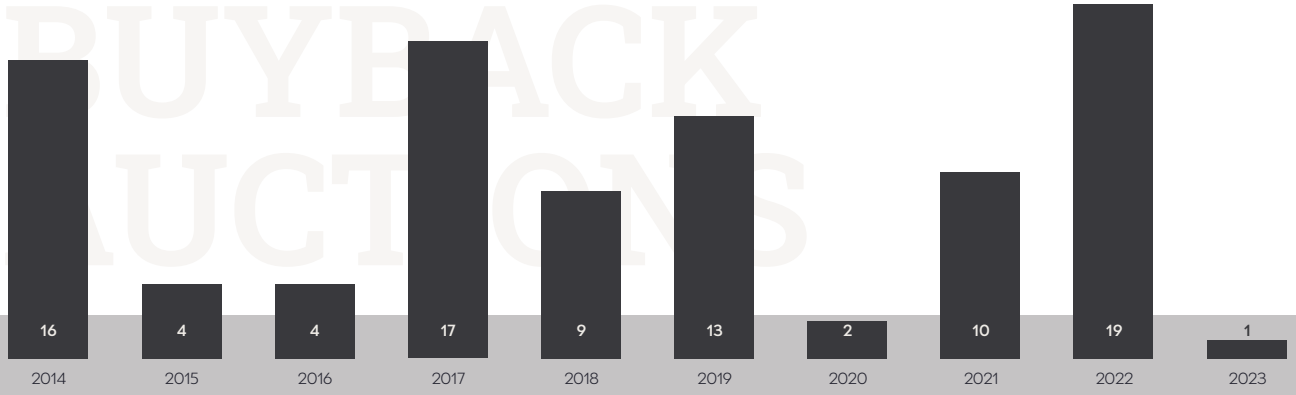
In buyback auctions, tradable securities are repurchased, mostly those with short-term maturities, and allowing for the partial early repayment of the security while reducing the total government debt. This differs from switch auctions, in which the redeemed securities are exchanged for other securities. Some Factors considered when selecting securities for repurchase include the impact on tradability of the security, savings in interest expenditures, and potential market demand.

The Primary Objectives of Security Repurchases:

- Efficient cash flow management
- Reduce refinancing risk
- Reduce budgetary interest payments
- Issuance and redemption smoothing

In 2023, the scope of government security buybacks substantially decreased due to the rise in financing needs. Total transactions amounted to roughly NIS 1.1 billion, compared to about NIS 19 billion of repurchases in 2022.

The graph below illustrates buyback auction sizes over the past decade:



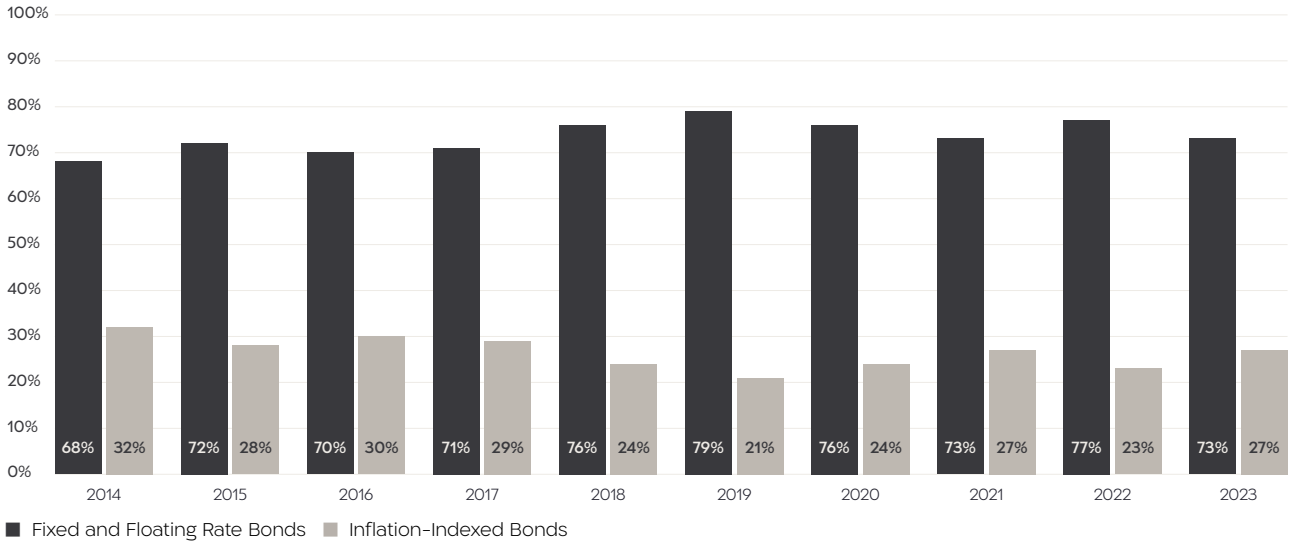
Short-Term Bonds

Short-term securities (with maturities of less than one year) are issued as a part of the cash flow management policy. The government issues short-term securities according to cash flow needs and market conditions. Different amounts are issued from month to month, depending on ongoing financing needs and considerations of efficient cash flow management.

Tradable Securities Issued on the Domestic Market in 2023

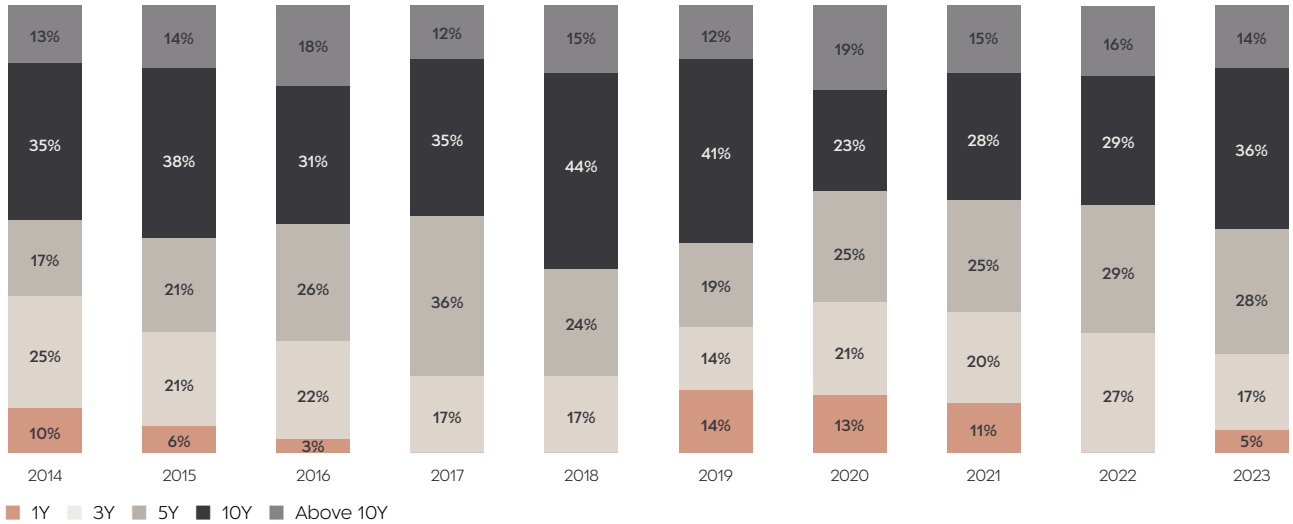
In 2023, capital was raised throughout the year through ongoing auctions and switch auctions. Most issuances in 2023 served to expand existing series (Tapping). In addition to the expansion of existing series, three new securities were issued during the year - two bonds with five-year maturities (one shekel-denominated and one CPI-linked) and one short-term bond that matures in August 2024.

The following graph illustrates the distribution of issuances by shekel-denominated and CPI-linked channels following. This distribution indicates that the shekel-denominated channel constituted the majority of capital raised over the years, in accordance with the policy of the Accountant General.



Domestic tradable debt is issued through short-term securities as well as benchmark maturities of 3, 5, 10, 20 and 30 years.

The following graph illustrates the distribution of funding by term to maturity.



Coverage Ratio

The coverage ratio is calculated by dividing the quantity of demand for a security (demand) by the amount issued of the same security (supply) in a given auction - reflecting the market demand for the security being examined.

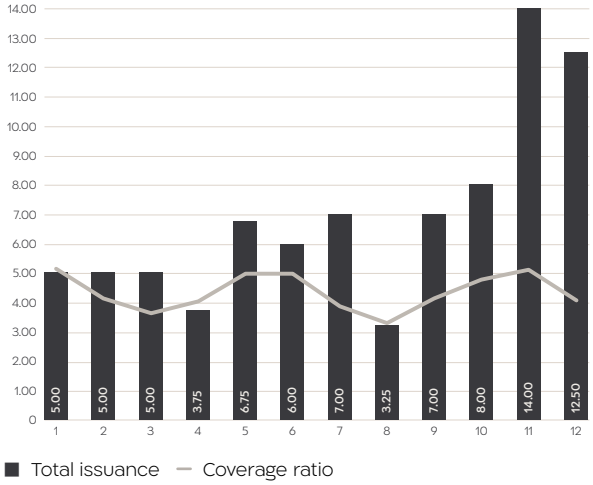
The following graph illustrates the coverage ratio (weighted average) alongside the amount issued per month.

The average coverage ratio for 2023 was roughly 4.4, compared to the average of 5.4 in 2022 and 4.9 over the past decade.

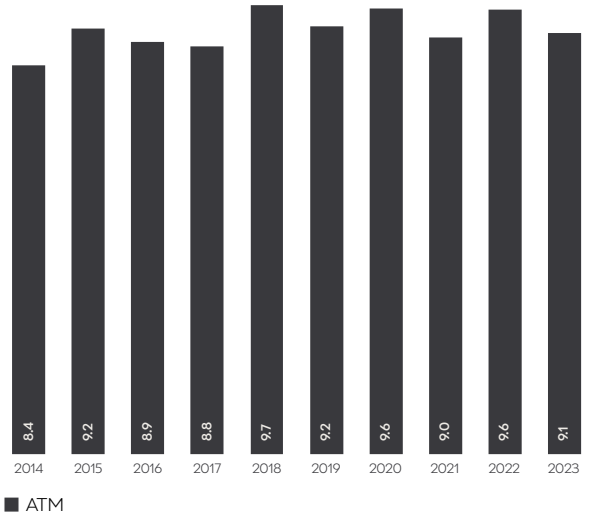
Factors that Influence the Coverage Rate:

- Domestic and global market conditions
- Investor needs
- Seasonal factors
- Funding types and sizes

Coverage Ratio and auction amount in 2023



The following graph illustrates the average term-to-maturity of the government's funding. Similar to previous years, this average is high at roughly 9.1 years.



New Series in the Domestic Market

As part of the government's multi-year debt management strategy, during 2024, the GDMU is expected to issue new On-the-Run securities.

The manner and timing of exchanging existing series will be determined by many factors, including the registered capital of the exchanged security, actual issuances of tradable instruments on the domestic market, average time to maturity of the exchanged securities, cash flow, and debt management considerations. It should be noted that the decision to issue these securities may change over the course of the year. The final notice regarding new securities being issued will be presented within the monthly capital raising plans of the GDMU.

GLOBAL MARKETS

The issuance of foreign-currency denominated debt in global markets serves several strategic objectives:

1. Diversification of financial resources for regular, ongoing needs, while enhancing access to capital for times of crisis
2. Expansion of the investor base for government securities
3. Exposure of the Israeli market to foreign investors

THE STOCK OF GLOBAL DEBT AS OF THE END OF 2023 AMOUNTED TO ROUGHLY NIS 180 BILLION, COMPARED TO ROUGHLY NIS 154 AT THE END OF 2022.

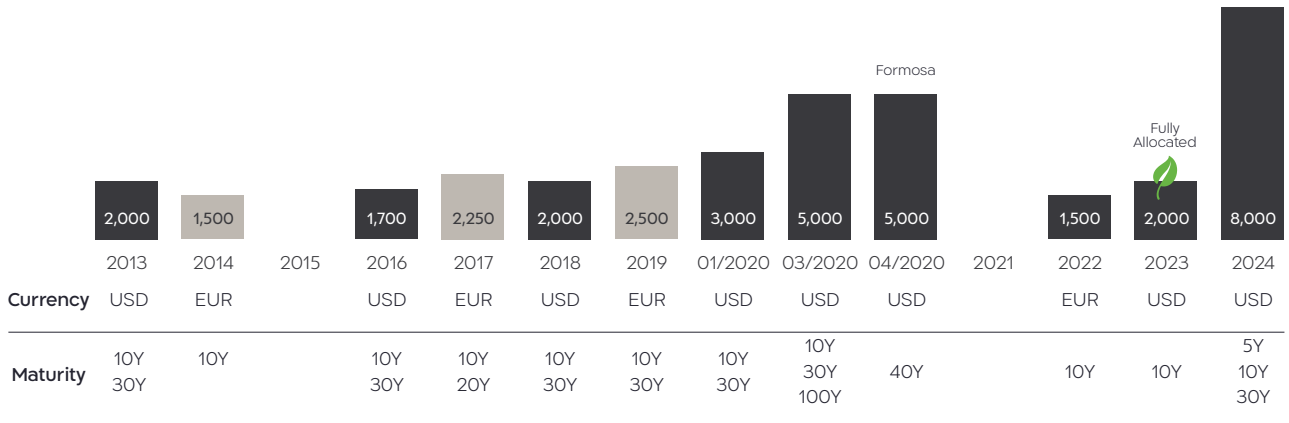
The increase is primarily due to extensive private issuances made in the last quarter of 2023 and changes in the exchange rate. The global market portfolio is comprised of public bonds, private offerings, debt offerings through the Israel Bonds Organization, past offerings guaranteed by the government of the United States, and other additional loans.

Sovereign Issuances

Between 1995 and 2023, the State of Israel issued 25 sovereign bonds in the global debt capital markets, including in the United States, Europe, Taiwan, and Japan. In the past decade, the amounts issued in global offerings have been trending upward due to the Accountant General's policy that prefers issuing benchmark series due to increased financing needs, among other factors.

The stock of sovereign bonds issued in foreign currencies at the end of 2023 amounted to roughly NIS 144 billion, compared to roughly NIS 112.5 billion at the end of 2022.

Global Public Issuances (USD/EUR Millions)



The State of Israel's First Green Issuance - January 2023

The State of Israel places great importance on promoting the steps and resources invested in aspects of sustainability, environmental protection, and climate change, both within public sector activity and government ministries as well as in the private and business sectors. In recent years, these have been advanced by publication of national action plans, climate objectives, promotion of government decisions, and legislation.

In January 2023, Israel returned to the USD market after approximately 3 years and executed, for the first time, a green issuance of USD 2 billion 10-year bond with a yield of 4.573%. This yield represents a spread of 95 basis points above the benchmark U.S. Treasury rate. The previous USD-denominated issuance was executed in 2020 during the COVID-19 pandemic, when the spread stood at more than 200 basis points for a similar term.

For the green bond offering, the State of Israel published its "Green Framework," a disclosure outlining the policies and objectives of the issuer, the expected use of proceeds for financing green projects that advance those objectives, the environmental benefits considered, and complementary information regarding the management of environmental risks associated with selected projects (the "Framework").

To comply with these principles, CICERO Shades of Green was chosen to provide a second-party opinion on the framework, ultimately assigning it its highest green score.

To formulate the framework and gather the necessary data for the issuance, an interministerial subcommittee was established by the Accountant General, consisting of representatives from Ministry of Finance, Ministry of Economy and Industry, Ministry of Transport, Ministry of Energy, Ministry for Environmental Protection, the Water Authority, and the Israel Innovation Authority.

This issuance, which was executed under the State of Israel's prospectus in the United States (SEC), attracted high demand, of more than six times the amount issued, from a diverse range of investors.

The Framework and allocation report of the Green Bond can be found on the Ministry of Finance website.[1]

Global Public Offerings - March 2024

In March 2024, the State of Israel issued dollar-denominated bonds via a public offering in international markets. Three bonds were issued with 5-, 10-, and 30-year maturities, totaling USD 8 billion. The spreads above the yields of the relevant benchmark U.S. Treasury rate were 135, 145 and 175 basis points, respectively. Demand for these offerings peaked at roughly USD 38 billion, 4.75 times more than the amount issued, and was the largest for the State of Israel's public debt offerings.

[1] https://www.gov.il/en/departments/publications/reports/green-bond-framework

Private Placements

An additional funding option available to the GDMU is the execution of private placements to strategic investors. These issuances may be executed under reverse inquiries from investors and the decision on their execution is made after an in-depth examination of funding needs, market conditions, and the quality of the investors.

Most private placements are executed by tapping existing series of bonds already issued in the global markets.

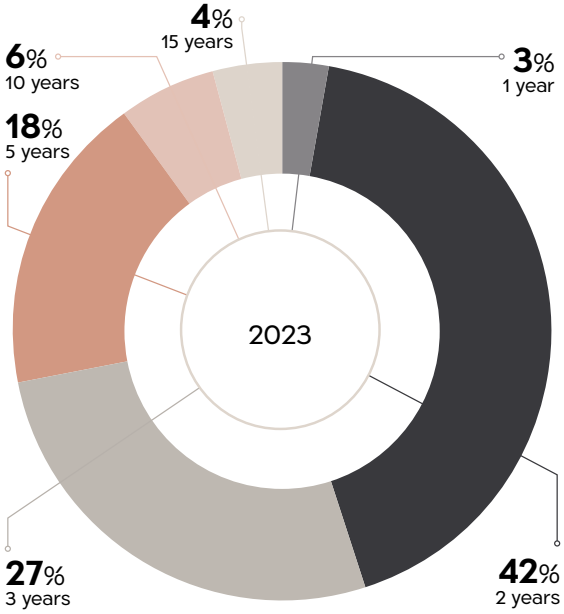
The "Iron Swords" war resulted in increased annual financing needs, particularly for 2023-2024. In this context, 14 private dollar-, euro- and yen-denominated offerings were issued in 2023, with the net capital raised amounting to roughly NIS 23 billion.

Issuances through the Israel Bonds Organization

Israel Bonds organization (State of Israel Bonds), established in the 1950s, serves as a platform for issuing non-tradable securities denominated in foreign currencies. It assists with the financing needs of the government and helps preserve the relationship between the State of Israel and Jewish diaspora. Over the years, the Israel Bonds organization has shown a counter-cyclical nature: in years of recession or geopolitical shock, the amount of debt raised by the organization increases. The organization's primary goal is to expand the investor base and diversify the funding sources of the State of Israel, mainly through retail customers, but also through institutions.

In 2023, the organization raised roughly USD 2.7 billion. In total, as of the end of 2023, the stock of debt raised through the Bond organization is approximately NIS 23.2 billion, compared to NIS 18.5 billion at the end of 2022.

Bonds Organization Funding by Time to Maturity (%)



United States Government Guarantees

In April 2003, the United States Congress approved a three-year program to provide up to USD 9 billion par value guarantees for debt issuance by the Israeli government. The United States provides a full guarantee for the principal and interest payments of bonds issued by Israel under this program, therefore these bonds benefit from a credit rating comparable to the credit rating of the United States and the yield at which they are sold is only slightly higher than the yield on U.S. government bonds. The program has been extended several times by the U.S. government, most recently in December 2022, until 2028.

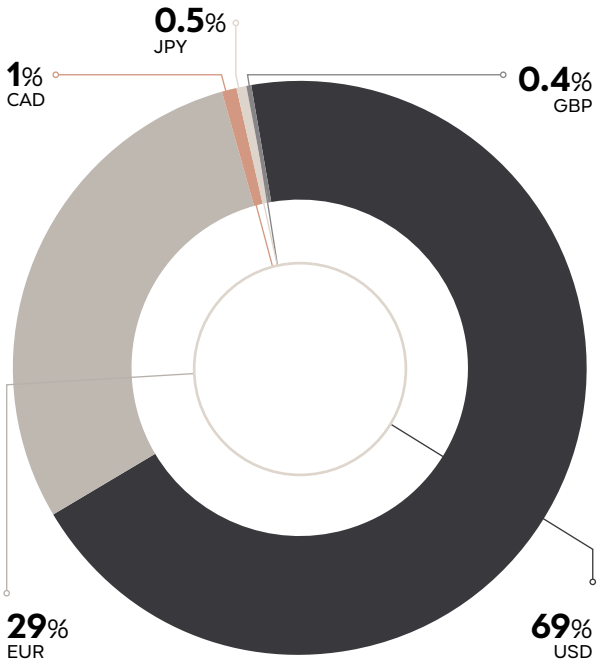
Under the guarantee program, in the years 2003- 2004, the State of Israel issued bonds with a par value of USD 4.1 billion. The Israeli government has not utilized the guarantee program since November 2004. As of the end of 2023, the balance available for use under the program totals USD 3.8 billion.

The U.S. guarantee program supports the fundraising capabilities of the State of Israel in international markets in times of emergency. To date, there is no intention to utilize the program except in the case of an essential financing need. The stock of bonds guaranteed by the U.S. government, as of the end of 2023, stands at roughly NIS 12.5 billion, compared to roughly NIS 21.5 billion at the end of 2022. This decrease is due to repurchases of bonds with this gurantee made in 2022, as well as exchange rate fluctations.

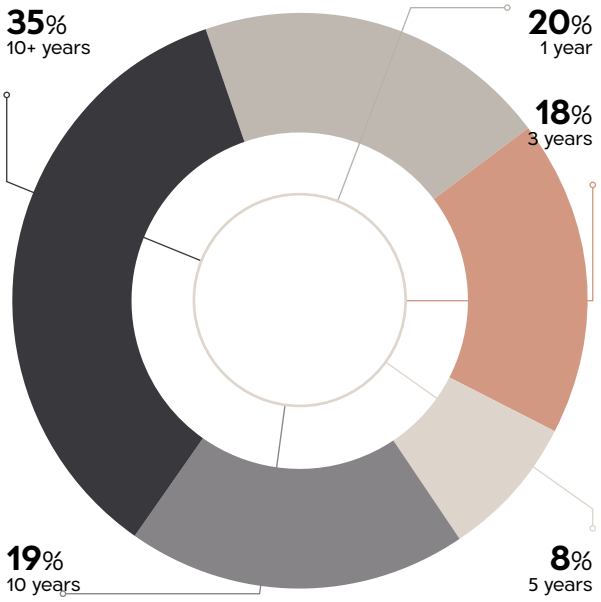
Loans from Foreign Governments and Other Loans

In addition, there is an additional balance of nontradable foreign currency debt consisting of bonds to foreign governments, international institutions, foreign banks, and bi-national funds. At the end of 2023, this balance amounted to roughly NIS 1.5 billion, compared to NIS 1.4 billion at the end of 2022, and it constitutes about 1% of the total foreign currency debt.

Debt Portfolio by Currency (%)



External Market Debt Portfolio by Maturity - Principal Only (%)



The State of Israel's Credit Rating

	Moody's	S&P	Fitch
Rating	A2	AA-	A+
Outlook	Negative	Negative	Negative

Following the outbreak of the "Iron Swords" war, Israel was placed under "Negative Rate Watch" by two rating agencies. In November 2023, S&P Global Ratings affirmed Israel's credit rating of AA-, but changed the outlook from "Stable" to "Negative". In October 2023, Fitch Ratings affirmed Israel's A+ rating and placed Israel on "Negative Rate Watch". In April 2024 Fitch removed Israel from "Rating Watch Negative", and changed Israel's rating outlook from "Stable" to "Negative". In April 2023, Moody's Investor Services affirmed Israel's A1 credit rating but updated Israel's credit outlook from "Positive" to "Stable", and in November placed Israel on "Negative Rate Watch". For the first time in Israel's history, in February 2024, Moody's downgraded Israel's credit rating to A2, and placed Israel on a "Negative" outlook.

Rating Agencies on Israel

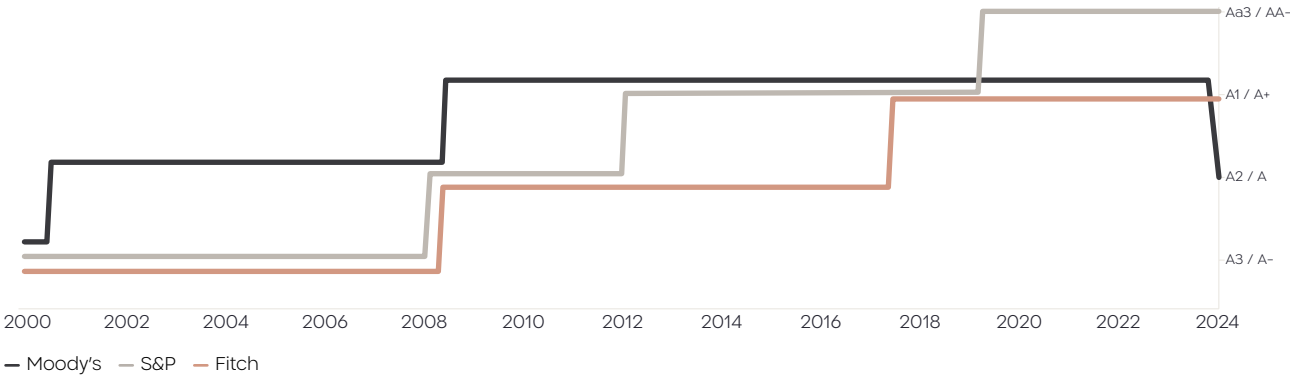
STRENGTHS

- Diverse economy that is financially robust, high added value.
- Strong external accounts.
- Flexible monetary policy and deep domestic markets.
- Top-tier access to capital markets, both domestically and globally.

CHALLENGES

- Lacking political stability, which negatively impacts policy making.
- Increased risk - both domestic security risk and regional geopolitical risk - is expected to continue to limit Israel's credit rating.
- Relatively high government debt-to-GDP ratio.
- Substantial income and education gaps between different population groups and demographic changes likely to hinder the growth potential of Israel in the long term.

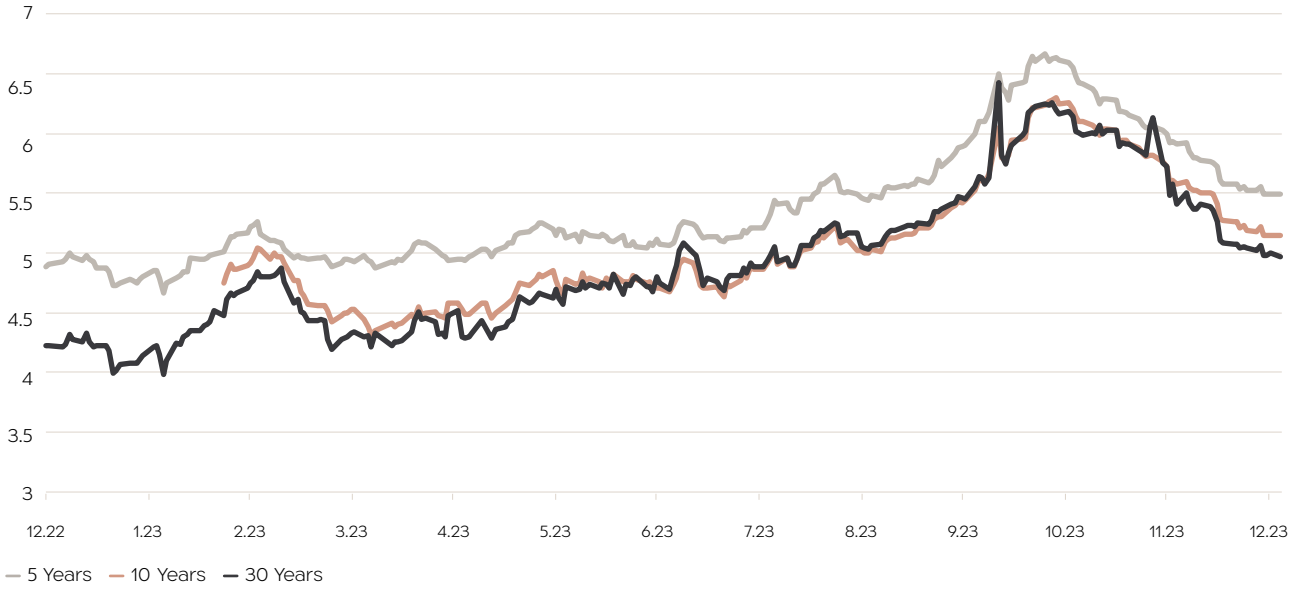
Development of Israel's Credit Rating



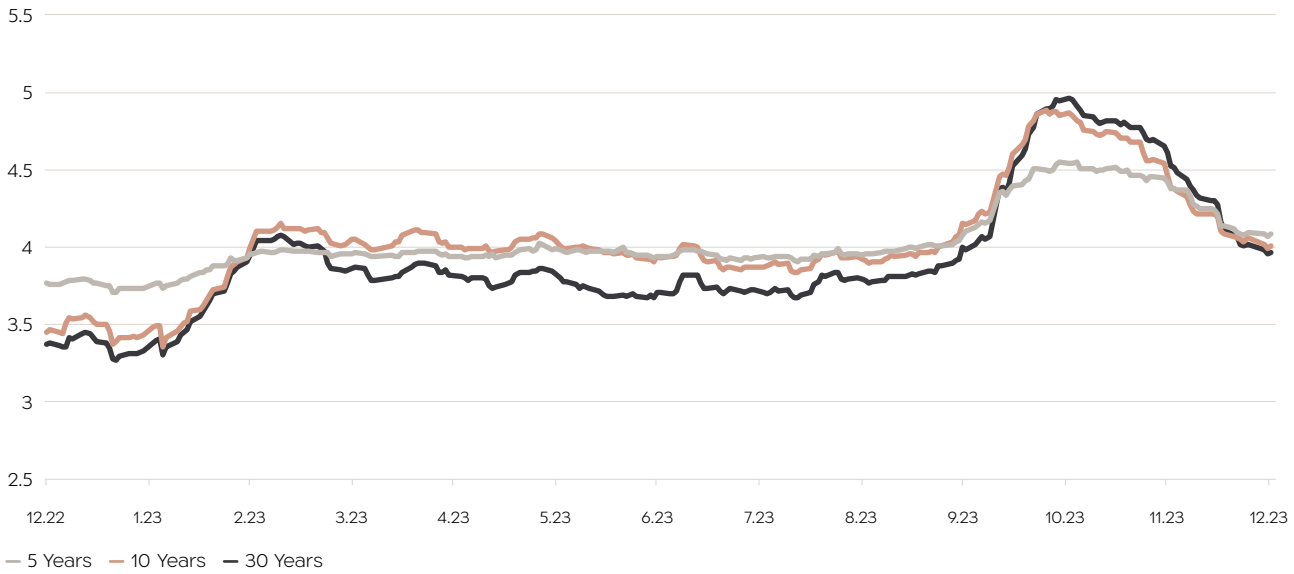
Yields on Foreign Currency Denominated Bonds Issued by the Israeli Government

The graph below illustrates bond yields in dollars and euros with maturities of 5-, 10-, and 30-years. The yields on these securities constitute the consolidation curve for domestic market risk.

The yield of treasury bonds in USD



The yield of treasury bonds in EUR



SECONDARY MARKET



Market Making in Government Bonds

The Primary Dealership Reform, which took effect in 2006, has several objectives: develop a competitive and efficient government bond market, facilitate the entry of international investors, increase demand for government bonds, and reduce financing costs.

Primary Dealers are required to fulfill obligations in both the primary and secondary markets and, in return, are entitled to benefits such as: reserved participation in issuances, participation in non-competitive auctions, access to the bond lending facility, and eligibility to act as a counterparty in hedging transactions.

IN 2023, THERE WERE 12 PRIMARY DEALERS OF GOVERNMENT BONDS, SEVEN OF WHICH WERE INTERNATIONAL BANKS.



Primary Market Rankings

Primary market rankings are based on the volume of purchases in government bond issuances. The rankings are calculated on a quarterly and annual basis.



Secondary Market Rankings for 2023

Secondary market rankings are based on trading data and price quotes from the primary dealer designated trading platform, MTS, for both the CPI-linked and the shekel (fixed-rate) channels. The rankings are calculated weekly, monthly, quarterly, and annually. The levels of primary dealers' participation in non-competitive auctions are determined based on weekly rankings.

	Yearly Primary Market Ranking Volume of purchases in issuance auctions, in NIS*	Yeraly Secondary Market Ranking - Nominal Activity in the MTS trading platform	Yeraly Secondary Market Ranking - CPI-linked Activity in the MTS trading platform
1	Discount	Leumi	Leumi
2	Leumi	Hapoalim	Hapoalim
3	Barclays	Discount	Discount
4	Hapoalim	Goldman Sachs	Goldman Sachs
5	Goldman Sachs	Mizrahi tefahot	Mizrahi tefahot
6	Mizrahi tefahot	Barclays	Barclays
7	Merrill Lynch	Deutsche Bank	JP Morgan
8	Deutsche Bank	JP Morgan	Citibank
9	Citibank	Citibank	Deutsche Bank
10	BNP Paribas	BNP Paribas	BNP Paribas
11	Fibi	Fibi	Fibi
12	JP Morgan	Merrill Lynch	Merrill Lynch

Trading Volume

Trading in government bonds takes place in parallel on several trading venues: the Tel Aviv Stock Exchange ("TASE"), the MTS (the designated trading platform for the Primary Dealers), and over the counter ("OTC").

In 2023, the government bond market saw higher trading volumes across all channels compared to 2022. The broader context for the rise in trading volumes is attributable to continued tightening of monetary policy in Israel and globally, elevated uncertainty relating to the impact of the proposals of legislative changes in Israel on the economy, and the "Iron Swords" war following the events of October 7, 2023, resulting in a higher risk premium in Israel. Together, these factors have heightened the volatility of government bond prices and led to a rise in trading volumes. The average daily trading volume of government bonds on the TASE was NIS 2.4 billion for 2023, an increase from the average of NIS 2.1 billion for 2022. The total trading volume in the TASE reached NIS 605 billion in 2023, compared to NIS 513 billion in 2022. On the MTS, the trading volume was NIS 43 billion in 2023, up from NIS 41 billion in 2022. OTC trading (non-TASE transactions) also increased, reaching approximately NIS 116 billion in 2023, compared to about NIS 81 billion in 2022.

TOTAL GOVERNMENT BOND TRADING VOLUMES DURING 2023 REACHED A DAILY AVERAGE OF ROUGHLY NIS 3.14 BILLION, AN INCREASE FROM APPROXIMATELY NIS 2.7 BILLION FOR 2022 (THE AVERAGE IS CALCULATED BASED ON TRADING DAYS ON THE TASE; MTS TRADING IS CONDUCTED MONDAYS THROUGH THURSDAYS).

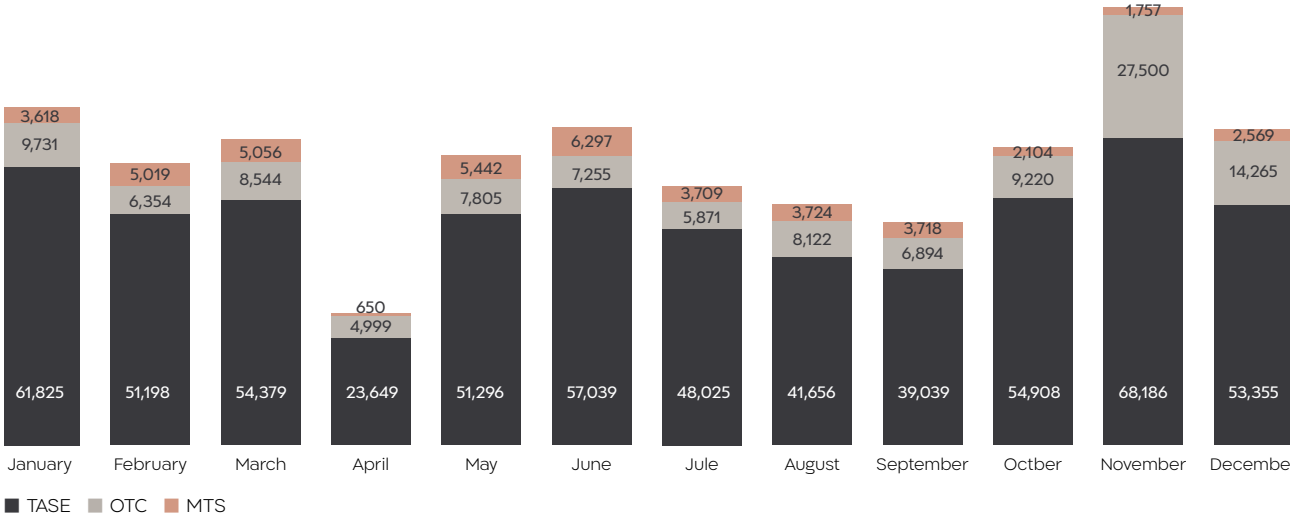
Distribution of trading volumes across venues:

TASE
79.05% of trading
(2022 - **79.73%**)

MTS
5.71% of trading
(2022 - **7.6%**)

OTC
15.24% of trading
(2022 - **12.65%**)

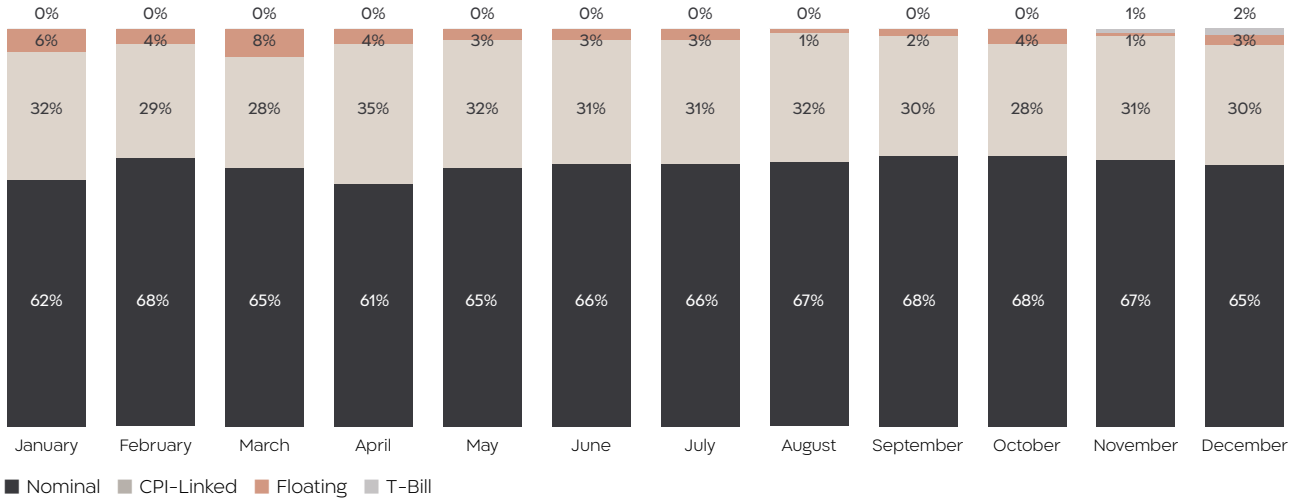
Trading Volumes of Government Bonds in 2023 (NIS millions)



Distribution of Trading by Channel

As in previous years, government bond trading in 2023 was concentrated in the fixed-rate NIS channel (not CPI-linked). Trading proportion for Each Channel: Fixed-Rate Channel: 65.92% (2022: 61.34%); CPI-linked Channel: 30.34% (2022: 34.78%); Variable Interest Channel: 3.42% (2022: 3.86%); Short-Term Bond Channel: 0.32% (2022: 0.03%).

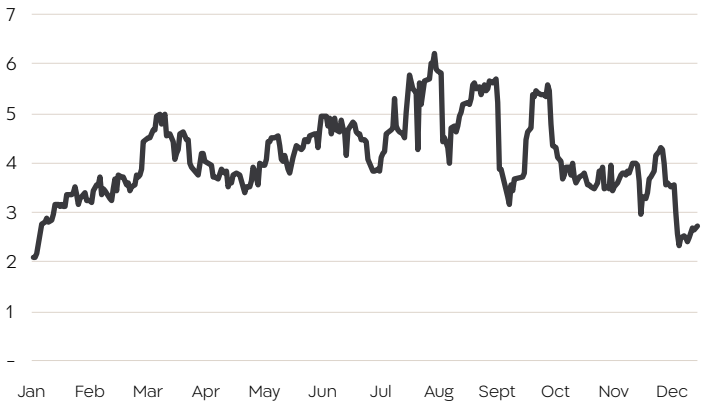
Breakdown of Trading Turnover in Different Segments



Bond Lending Facility

The bond lending facility began in September 2006 as part of the Primary Dealership Reform. The Ministry of Finance established the bond lending facility, together with the TASE Clearing House, to allow Primary Dealers to borrow government bonds. Each Primary Dealer may borrow up to NIS 1.5 billion of government bonds, and must provide monetary deposits as collateral if it wishes to exercise that right. Primary Dealers are charged a borrowing fee for bond lending transactions in accordance with the Ministry's bond lending protocol. **In 2023, the lending facility ranged between NIS 2.1 - 6.2 billion (market value of borrowed bonds).**

Borrowing balance (NIS, billions)



Distribution of Holdings in Tradable Government Bonds

Notable Data:

32.6%

Holdings of pension and provident funds in tradable government bonds decreased to 32.6% in 2023, compared to 33.3% at the end of 2022.

12%

Holdings of the Bank of Israel in tradable government bonds decreased to 12% in 2023, compared to 13% in 2022.

15%

Holdings of foreign investors in tradable government bonds increased to 15% in 2023, compared to 12.1% at the end of 2022.


70.
26.417
12.002
06.381

DEBT PORTFOLIO

5

Government Debt

At the end of 2023, the government debt portfolio amounted to roughly NIS 1,127 billion, compared to roughly NIS 1,037 billion at the end of 2022, marking an estimated 8.7% increase in the debt portfolio.

The government in 2023 saw an increase in financing needs, primarily during the last quarter of the year, as a result of the "Iron Swords" war and its economic impact. In line with this, the amount of capital raised in government debt offerings increased from roughly NIS 63 billion in 2022 to roughly NIS 160 billion in 2023. Out of this total, roughly NIS 116 billion was issued in the tradable domestic market, roughly NIS 40 billion was raised on external markets, and roughly NIS 5 billion was raised in the non-tradable domestic market.

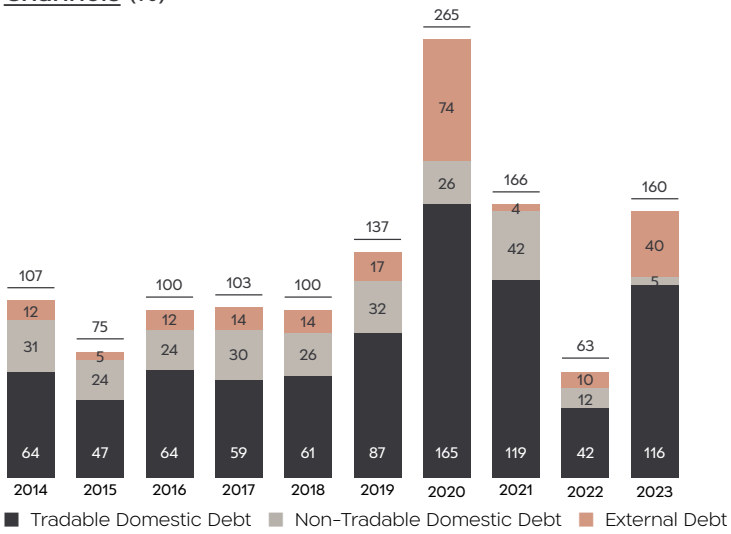
Issuances in the tradable domestic market during 2023 constituted roughly 72% of the annual capital raised, and stands at about NIS 116 billion, compared to about NIS 42 billion raised in tradable domestic debt for 2022 (roughly 65% of the annual capital raised in 2022). As of the end of 2023, the tradable domestic debt outstanding comprises roughly 54% of the government's debt portfolio.

Issuances in external markets during 2023 constituted about 25% of the annual capital raised, and amounting to about NIS 40 billion, compared to about NIS 10 billion raised in external markets during 2022. During 2023, roughly NIS 30 billion in private and public debt offerings were made on external markets. In January 2023, benchmark offerings of US dollar-denominated bonds with 10-year maturities were issued, and 14 private debt offerings denominated in USD, EUR, and JPY were issued in the final quarter. In addition, capital raising via the Israel Bonds Organization amounted to roughly NIS 10 billion. At the close of 2023, external debt accounted for roughly 16% of the total government debt.

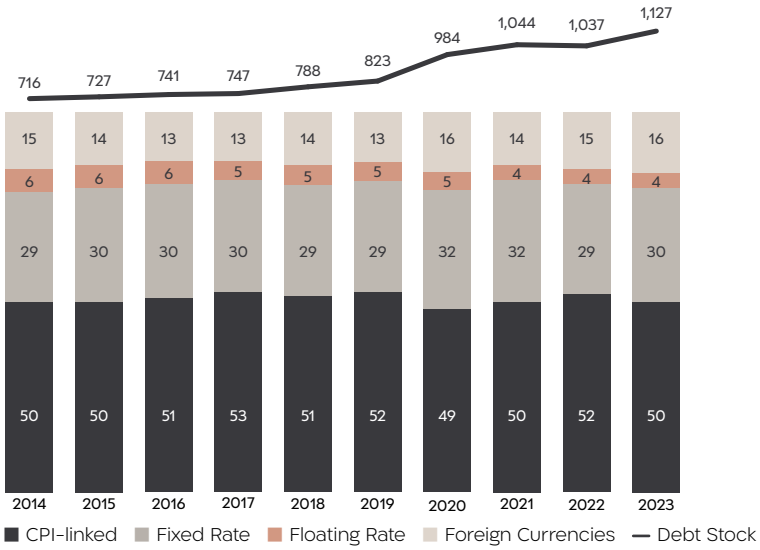
Offerings of CPI-linked debt are issued through tradable and non-tradable domestic channels. During 2023, following the reform ending designated bond issuances, non-tradable domestic issuances, all of which are CPI-linked, declined sharply to just 3% of total government debt issuance, a notable decrease from roughly 19% during 2022. This channel of capital raising amounted to only about NIS 5 billion, solely for insurance policies and legacy debt. Issuances of CPI-linked tradable domestic debt amounted to roughly NIS 31 billion and constituted around 20% of the total government debt issuance in 2023, compared to roughly 15% in 2022.

In 2023, the rate of CPI-linked debt stock decreased to around 50%, as opposed to around 52% in 2022, despite a 3% annual rate of inflation. This decline is attributable to the net positive increase in issuing of non-CPI-linked debt compared to CPI-linked debt.

Total Government Issuances and Distribution Across Channels (%)



Government Debt Portfolio and Distribution by Linkage (%)

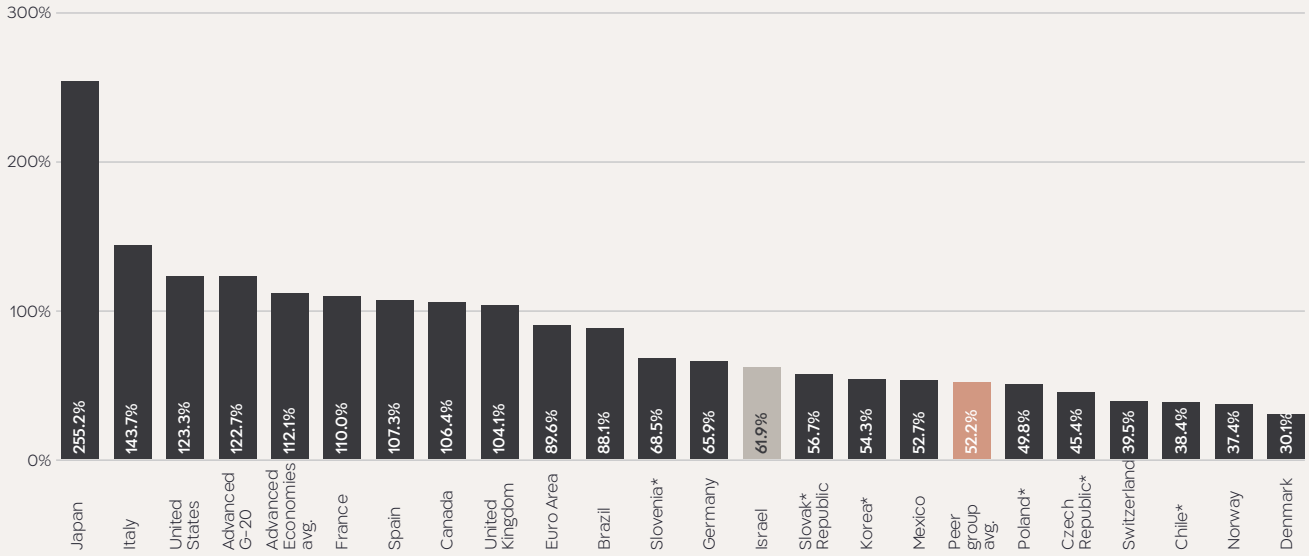


Debt-to-GDP Ratio

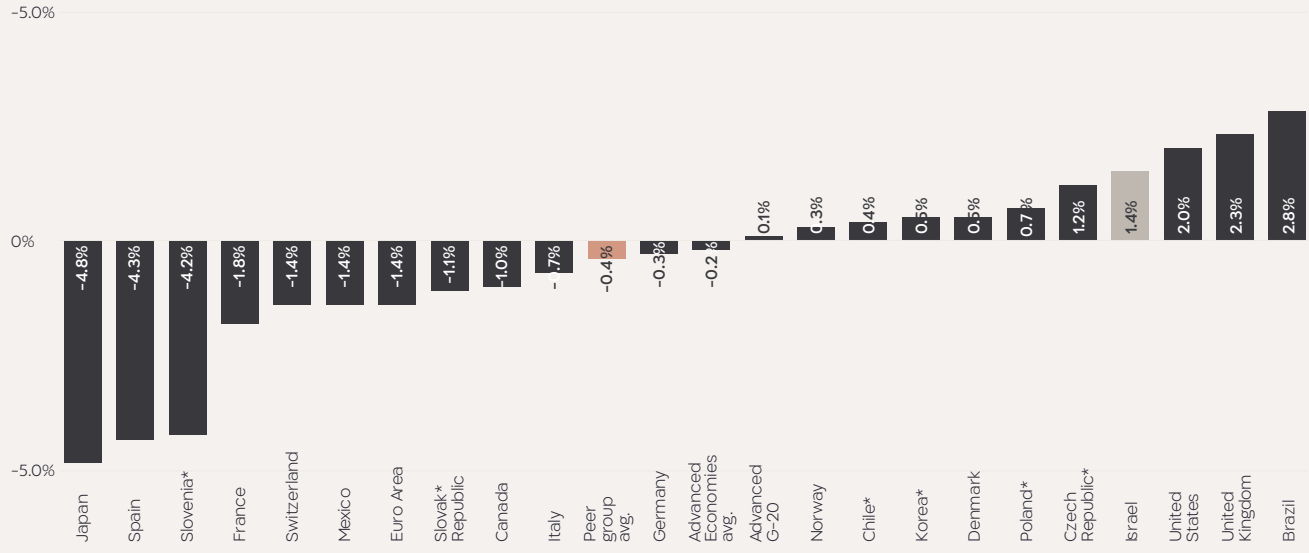
The debt-to-GDP ratio is a key metric used by credit rating agencies and serves as an indicator of the State's financial stability and fiscal flexibility.

In the decade leading up to the COVI9-10 pandemic, the debt-to-GDP ratio was on a downward trend due to responsible fiscal policy and efficient debt management, among other factors. In 2023, heightened financial needs following the outbreak of the "Iron Swords" war in the last quarter led to an increase in the government debt-to-GDP ratio. In 2023, the government debt-to-GDP ratio increased by roughly 1.5% compared to 2022, amounting to roughly 60.3%. The public debt-to-GDP ratio increased by approximately 1.4%, reaching roughly 61.9%.

Public Debt-to-GDP Ratio, 2023



Change in Public Debt-to-GDP Ratio, 2022-2023



The graphs above indicate the debt-to-GDP ratio of public debt for 2023 rose by approximately 1.4%, in contrast to the average decrease of roughly 0.4% in the debt-to-GDP ratios of the peer countries. The increase can be attributed to the "Iron Swords" war, which led to a rise in government debt, coupled with a decrease in the growth rate compared to 2022. However, it is notable that the government debt-to-GDP ratio has remained low relative to the average among developed economies and the average of the Euro Area.

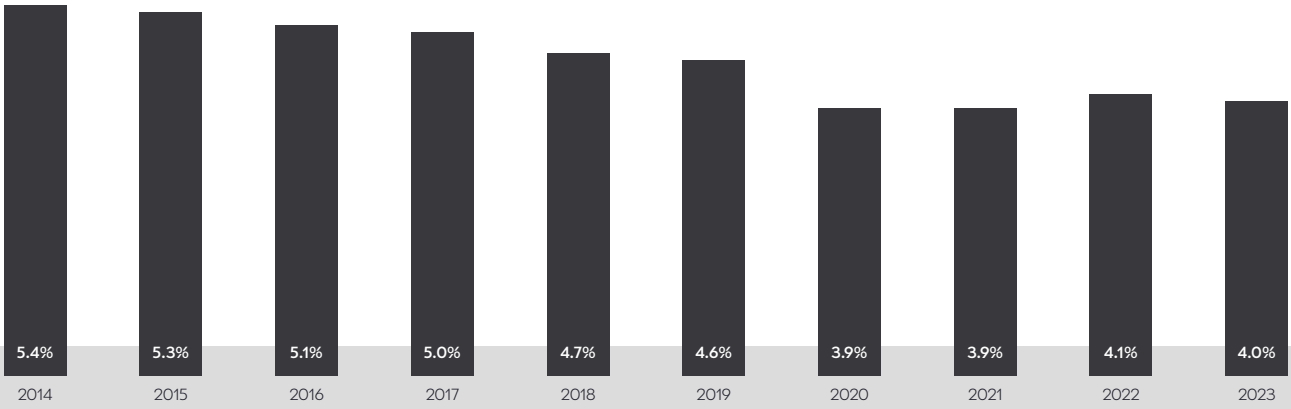
*Peer countries

Interest Expenses

Interest expenses in 2023 amounted to roughly NIS 44.7 billion, compared to roughly NIS 42.1 billion in 2022. Government expenses in 2023 amounted to approximately NIS 516 billion, compared to about NIS 459 billion in 2022. Despite the nominal increase in interest expenses, the proportion of interest expenses decreased to 8.7% of total government expenditures, compared to roughly 9.2% in 2022.

As illustrated in the graph below, the ratio of interest expenses to total government debt has been on a downward trajectory over the last ten years, decreasing from roughly 5.4% in 2014 to about 4.0% in 2023. This downward trend persisted between the years 2022 and 2023, due to the government debt increasing at a higher rate than interest expenses did in the corresponding period.

Interest Expenses to the Government Debt Ratio, 2014-2023



→

The graph below compares interest expenses between 2022 and 2023, for every channel, relative to the debt portfolio of each channel.

Tradable Domestic Channel: Interest expenses increased by roughly NIS 0.6 billion, from NIS 12.0 billion to NIS 12.6 billion. The interest expense rate as a percentage of the total tradable debt increased from 2.1% to 2.2%.

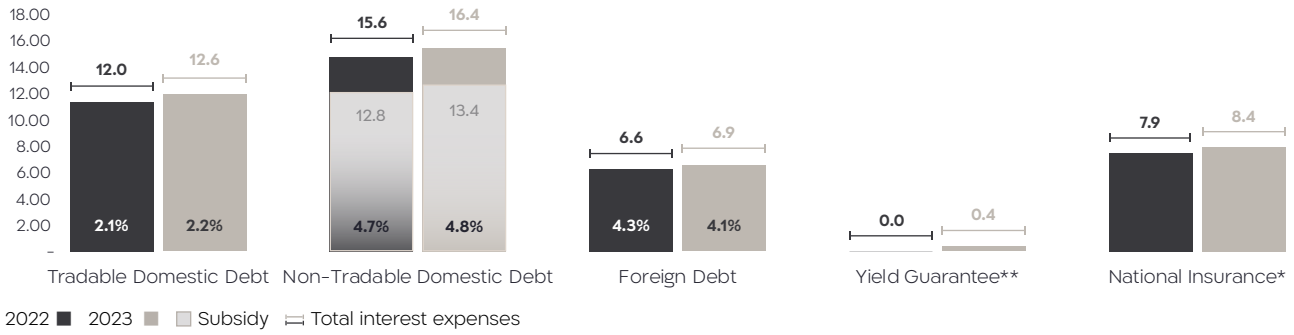
Non-Tradable Domestic Channel: Interest expenses increased by roughly NIS 0.7 billion, from NIS 15.6 billion to NIS 16.3 billion. The interest expense rate as a percentage of total non-tradable debt increased from 4.7% to 4.8%. The estimated subsidy of non-tradable bonds issued ,as required by law, to the pension funds and insurance companies amounted to roughly NIS 13.4 billion, compared to roughly NIS 12.8 billion in 2022. The subsidy attributed to pension funds in 2023 amounted to roughly NIS 11.3 billion, compared to roughly NIS 10.8 billion in 2022. The subsidy attributed to insurance companies ("Hetz" bonds) in 2023 amounted to roughly NIS 2.2 billion, compared to roughly NIS 2.1 billion in 2022.

External Channel: Interest expenses increased by roughly NIS 0.3 billion, from NIS 6.6 billion to NIS 6.9 billion. The interest expense as a percentage of the total external debt decreased from 4.3% to 4.1%.

Yield Guarantee Mechanism: The budgetary provision for the guarantee of yields from pension funds (the replacement mechanism of the "Arad" bonds) amounted to roughly NIS 0.4 billion.

National Insurance: Interest expenses increased by NIS 0.5 billion, from roughly NIS 7.9 billion to about NIS 8.4 billion.

Total Interest Expense, and Interest Expense-to-Dept Ratio, Distribution by Channel 2022-2023



*The National Insurance debt is not recognized as government debt because the State does not issue debt instruments to cover it. Nevertheless, this debt is accounted for in the State budget and is subject to fiscal regulations.

**Budgetary allocation for a designated fund in accordance with the amendment to the Financial Services Supervision Act (Provident Funds), 2005.

Government Debt Risk Management

The primary risks of the government debt portfolio are refinancing risk, liquidity risk, market risk, and credit risk. Risk management is implemented through a structured policy within the framework of strategic long-term goals for debt management, the treasury, and government liquidity. Risk management strategies are implemented based on models, scenarios, and simulations conducted to assist in mitigating economic and budgetary risks.

Primary Financial Risks:

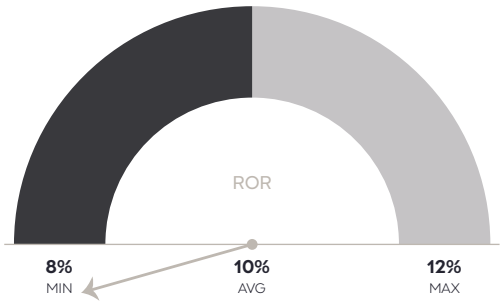
1

REFINANCING RISK

The risk that the State will not be able to meet its obligations to pay past debt or will have to refinance the debt at elevated costs. This is the primary risk associated with managing the government's debt portfolio. Consistent offerings issued at a comparable scope, annually and monthly, creates certainty for both decision-makers and capital markets actors, increases market demand, which enables economically efficient debt refinancings and reduces refinancing risk. In addition, extending the ATM for government debt and monitoring the ROR further mitigate this risk.

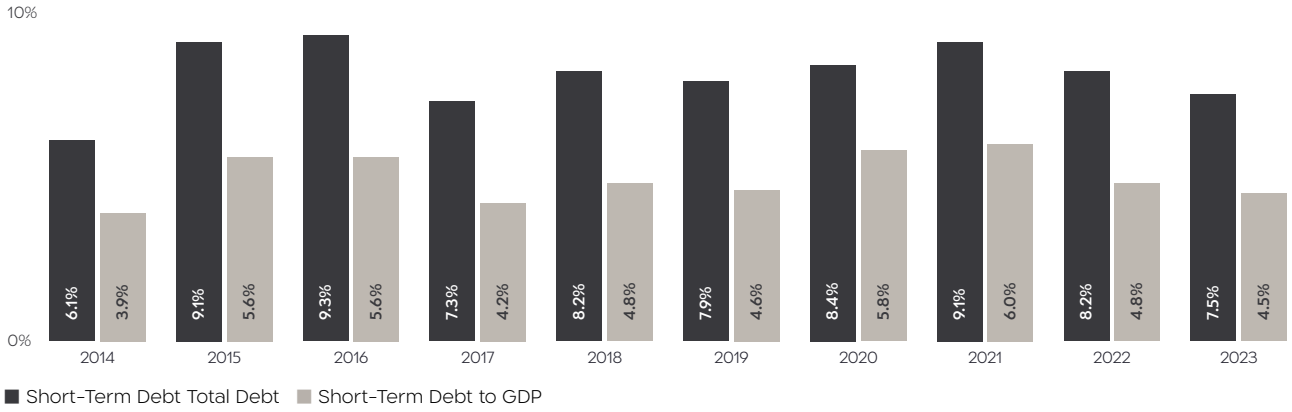
Refinancing Risk is Estimated Through Several Metrics:

→ Examining short-term debt (debt due for repayment in the next year) relative to the total debt ("Rollover Ratio"). The risk management policy targets a range between 8% and 12%.

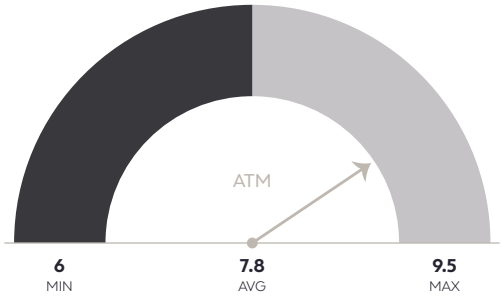


This metric during the third quarter of 2023 amounted to roughly 8.1%. The debt issued during the last quarter of 2023 had relatively longer maturities, bringing the rate down to 7.5%. Furthermore, the ratio of short-term debt-to-GDP was only slightly lower than 2022, amounting to 4.5% in 2023 compared to 4.8% in 2022. In 2024, the ROR is expected to return to the targeted range.

Short-Term Government Debt to Total Debt and to GDP for 2014-2023

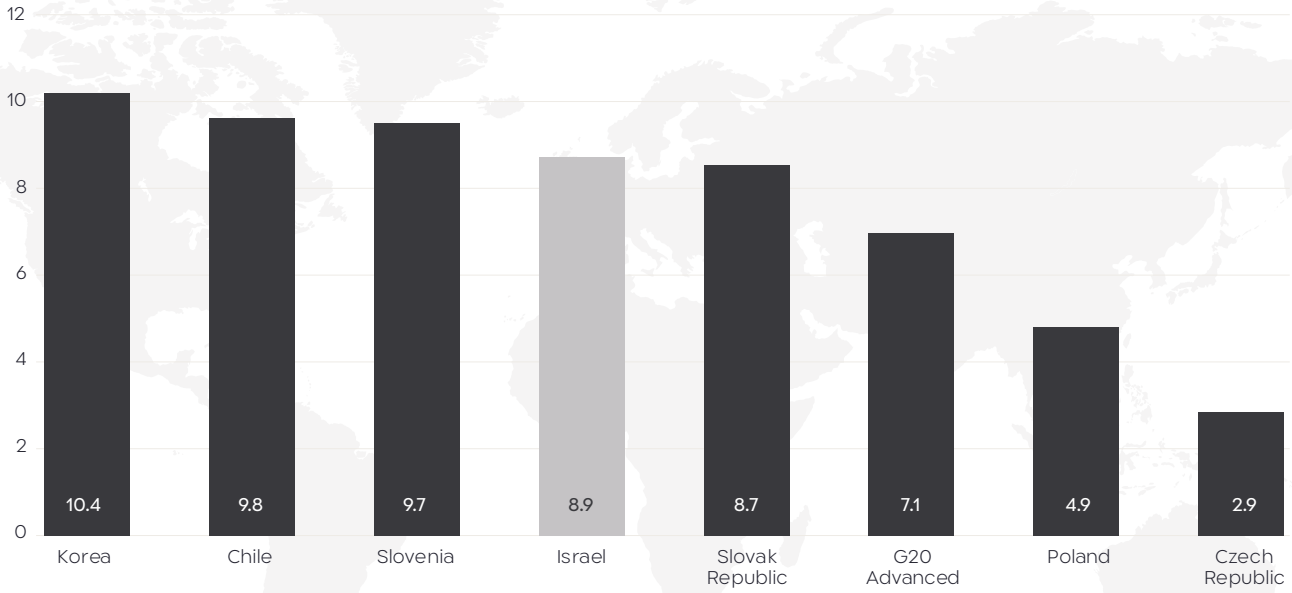


→ Average Time to Maturity (ATM) - This metric reflects the average lifespan of the debt portfolio and is calculated using a weighted average of the maturity dates for all outstanding principal debt. Because this is an average, ATM is an incomplete estimation of the risk; therefore the GDMU examines it in conjunction with the ROR for the next year and next three years. This integration between metrics allows for an estimation of refinancing risk. As of the end of 2023, the ATM fell to 8.9 years from 9.3 years at the end of 2022. The debt issuance strategy in recent years aimed to gradually extend the ATM and government debt maturities to around 9 years, as well as maintain the targeted ROR range as indicated above.



In a comparative analysis among relevant countries, the debt portfolio's ATM is situated between reference countries and is higher than the benchmark for developed economies.[1]

International Comparisons of ATM



[1]Source: The Ministry of Finance and the Bank of Israel, for the other countries - Fiscal Monitor, October 2023.

Several models are used to manage refinancing risk:

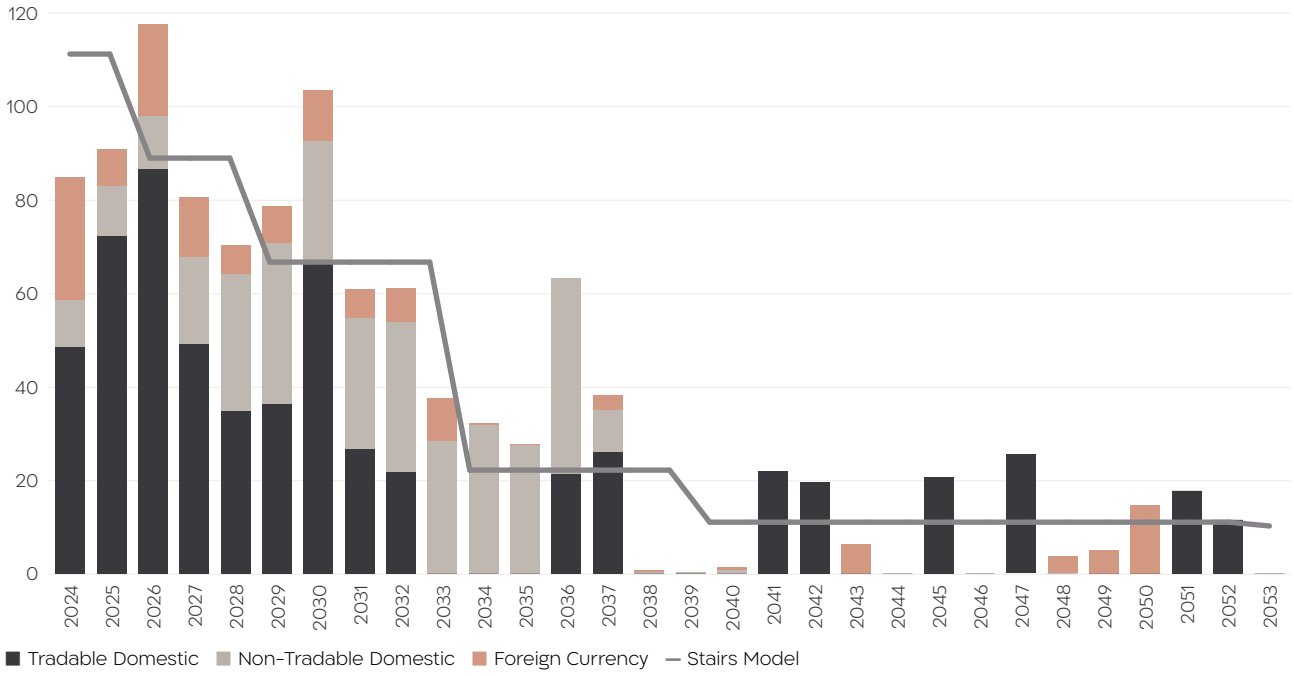
→ Issuance Framework (Stairs) - The Accountant General's Government Debt Management Unit ("GDMU") implements a long-term strategy in domestic and external tradable debt through the stairs model:

Gradual Redemption Curve - Utilizing a multi-year and gradual redemption structure.

Fixed Issuance Policy - Performing a fixed issuance policy such that a fixed quantity of issuances is made to benchemarks of 3, 5, 10, and 30 years while planning the gradual redemption curve.

Steady State - Planning and maintaining the existing redemption schedule.

In addition, the GDMU spreads out issuances throughout the year, through pre-planned issuances, switch and buyback auctions, and the use of short-term instruments for cash flow management, while ensuring adequate liquidity is maintained annually.



→ Fixed model for short-term bonds - Issuing new bonds with maturities up to one year to smooth the redemption schedule.

2

LIQUIDITY RISK

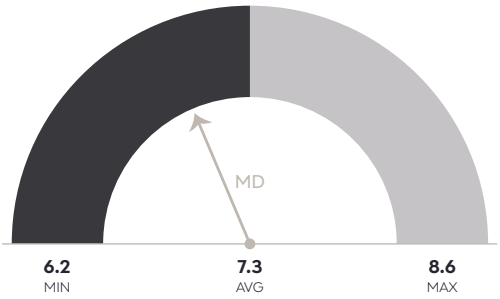
The risk that existing financing resources will not sufficiently cover the needs of the State at any given time. This risk is estimated and managed through models, scenarios (primary, stress, and extreme scenarios), and simulations conducted and monitored daily. In addition, the GDMU utilizes different liquidity instruments including short-term bonds, switch and buyback auctions. The State of Israel maintains liquidity reserves which matches the risk management strategy, while addressing the discrepancy between income and expenditures and ensuring that the treasury exceeds the minimum required to be prepared for different potential scenarios.

3

MARKET RISK

The risk of changes in government debt and interest expenditures as a result of market changes (indexes, interest rates, and currency exchange rates). This risk is estimated by the use of models, scenarios, and simulations and managed through hedging the exposure by using financial instruments (such as forward transactions).

→ Modified Duration - A metric that indicates the influence of interest rates on the market value of debt. The modified duration of government debt decreased to 6.9 years for 2023 from roughly 7.4 years in 2022.



→ Sensitivity to Consumer Price Index (CPI) - CPI-linked debt constituted around 50% of the portfolio at the end of 2023, thus the main sensitivity of the debt portfolio is its exposure to inflation. A change of 1% in the CPI results in an estimated adjustment of NIS 5.6 billion to the debt portfolio's absolute value.

→ Sensitivity to Currency Exchange Rates - debt denominated in other currencies constituted around 16% of the portfolio as of the end of 2023, exposing that debt to exchange rate fluctuations, which can impact both the debt portfolio and interest payments that are unhedged. In order to minimize exchange rate risk, the GDMU conducts hedging transactions.

Sensitivity of the Government Debt

	Change in Government Debt (NIS millions)	**Change in Debt-to-GDP Ratio for Government Debt** (% GDP)
Increase in the consumer price index (1%)	5,634	0.30%
Increase in the USD-NIS exchange rate (1%)	1,155	0.06%
Increase in the EUR-NIS exchange rate (1%)	612	0.03%

4

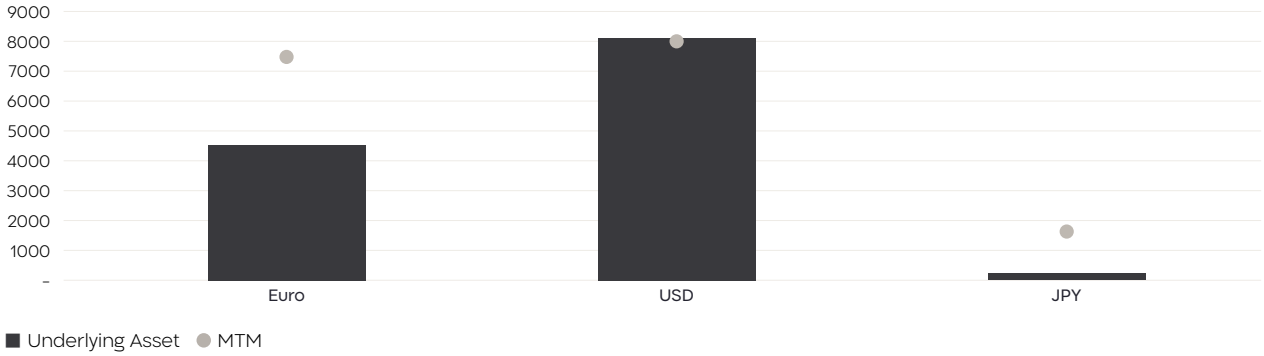
CREDIT RISK

Performing hedging transactions by the state exposes the government to credit risk in the event of a counterparty's insolvency. The primary objective of the hedging policy is to reduce the interest expense budget's exposure to exchange rate as a means of market risk management. Hedging transactions are divided between long-term through Cross-Currency Swaps and short-term through Forward and FX Swaps. In 2023, the GDMU conducted hedging transactions against principal and interest payments totaling an estimated USD 4.5 billion, EUR 3.9 billion, and JPY 20 billion.

To minimize the impact of credit risk, the State only conducts hedging transactions with primary market dealers under a signed CSA agreement and ISDA contract. This agreement requires a weekly calculation for the transfer of securities based on the fair market value of the trades. This transfer of securities assists in reducing exposure to the insolvency risk of the counterparty.

As of December 31, 2023, the government's hedging portfolio totaled roughly USD 12,886 million (the hedged amount). The mark-to-market value of all the positions as of December 31, 2023, reflects a financial advantage to the State's benefit of roughly USD 133 million.

Hedging Transactions and Fair Market Value



5

ADDITIONAL MODELS FOR GOVERNMENT DEBT RISK MANAGEMENT

→ Risk Cost Model - Analysis of the risk and cost associated with short, medium, and long-term issuance policies.

→ Debt Structure Simulation - Conducting financial modeling simulations of government bond debt development over the short, medium, and long-term, accounting for central risks and evaluating different issuance strategies.

→ Debt-to-GDP Forecast - The Debt-to-GDP ratio is a key indicator of the State's financial stability. Forecasting scenarios of varying debt-to-GDP developments under diverse market and macro-economic conditions assist in the optimization and management of government debt.

→ Financial Pricing Mechanisms - Pricing of debt, executing hedging transactions, and more, are conducted through the use of various financial models.

→ Interest Payment Forecast - This forecast is projected using the bottom-up approach and spreads present payments in accordance with anticipated market changes in Israel and abroad, including projections from changes in repayment schedules (new issuances, swaps, and reverse offerings).

→ Estimating additional risks to map and monitor financial risks comprehensively.

Average Issuance Amount and Number of Series

In accordance with the Accountant General's debt management policy, measures are taken to reduce the number of government bond series while increasing the volume of existing series. During 2023, two new bonds were issued in the domestic tradable market:

- ILGOV 0229 with maturity in 2029 as a 5-year shekel benchmark.
- ILCPI 1028 with maturity in 2028 as a 5-year CPI-linked benchmark.

In addition, in 2023, the short-term debenture series 0824 was issued.

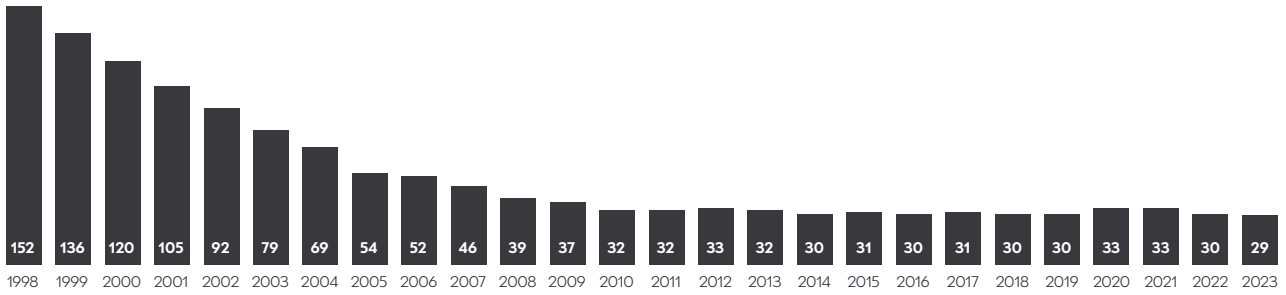
Additionally, as part of the above strategy, in 2023, the GDMU continued exchanging on-the-run bonds with off-the-run bonds (such that the latter, in effect, becomes on-the-run). The following are the bonds:

- ILGOV 0425 was exchanged for ILGOV 0825 as a 3-year shekel benchmark.
- ILGOV 0825 was exchanged for ILGOV 0226 as a 3-year shekel benchmark.

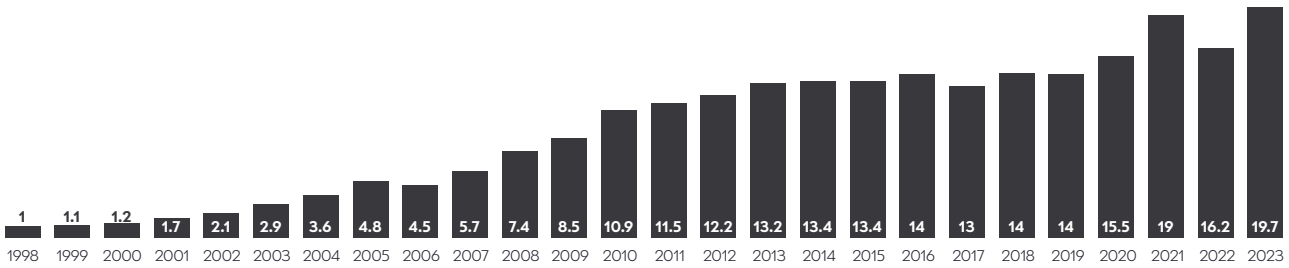
In 2023, four bond series reached maturity. Accordingly, the total tradable series outstanding contain 29 bonds, a decrease from 2022.

As can be seen in the graph below, over the years, the number of tradable bond series has substantially declined, while the average size of each series upon issue has increased. This policy improves the tradability and liquidity of the bonds and contributes to efficient planning of the redemption curve for government debt.

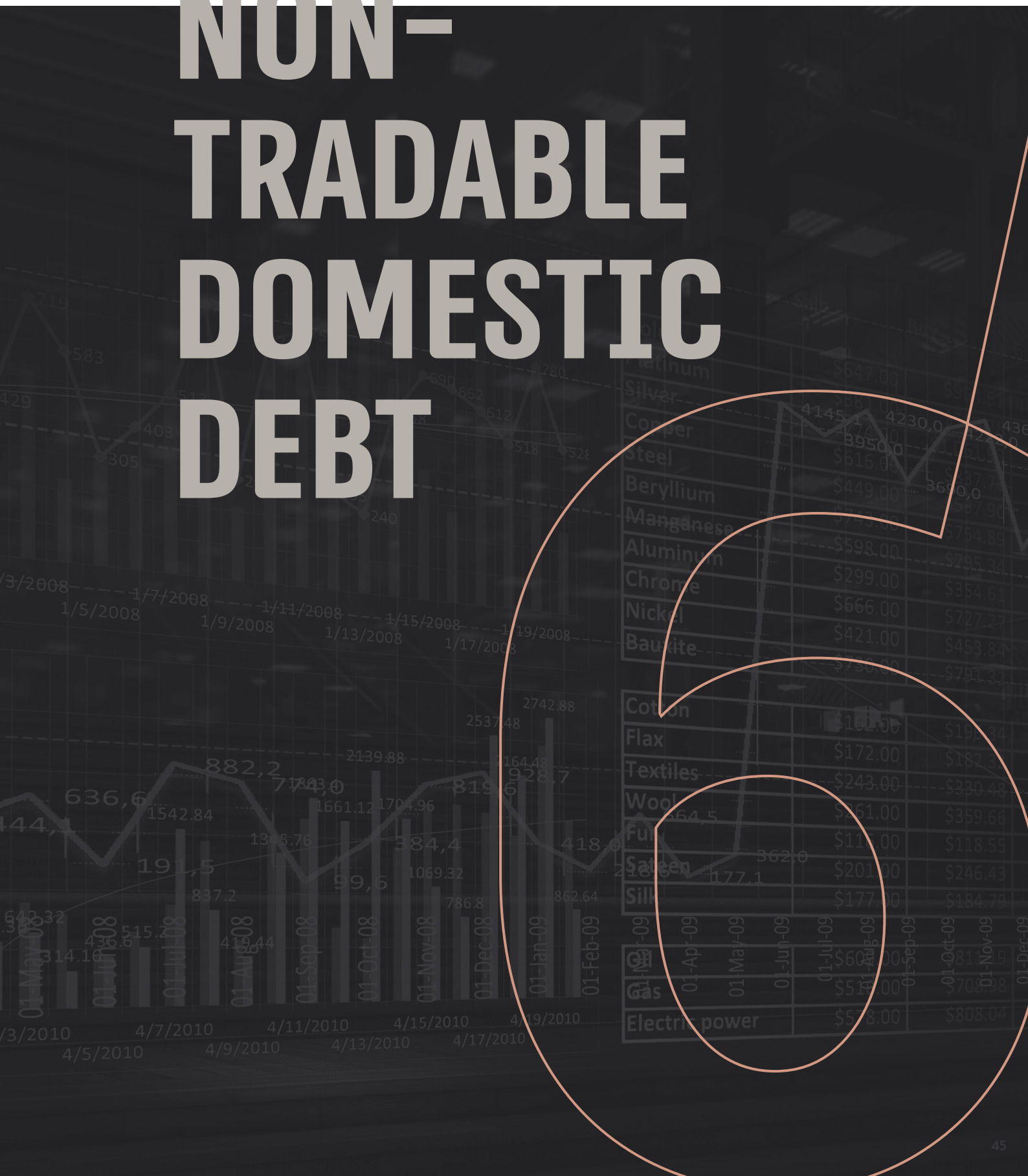
Number of Tradable Series in 1998-2023



Average Series Size in 1998-2023



NON-TRADABLE DOMESTIC DEBT



Non-Tradable Domestic Debt

In 2023, the total amount of non-tradable domestic debt was roughly NIS 4 billion. This debt was raised using the following instruments:

1. **Designated bonds for pension funds ("Arad")** - No issuances were made through this instrument in 2023 due to the designated bond reform[1], however, the redemption of these bonds totaled NIS 1.9 billion.

2. **Designated bonds for life insurance companies ("Hetz")** - From 1965 to 1990, non-tradable bonds for life insurance companies called "Hetz" (life-linked) were issued and featured a guaranteed yield. They had a fixed interest rate linked to an index, yielding between 4.0% and 6.2%. In the early 1990s, new entrants were excluded from receiving these bonds. In 2023, the volume of "Hetz" bonds issuances was roughly NIS 4.0 billion, an increase of nearly 8.2% compared to NIS 3.7 billion in 2022. This resulted in a negative net raise of approximately NIS 1.5 billion.

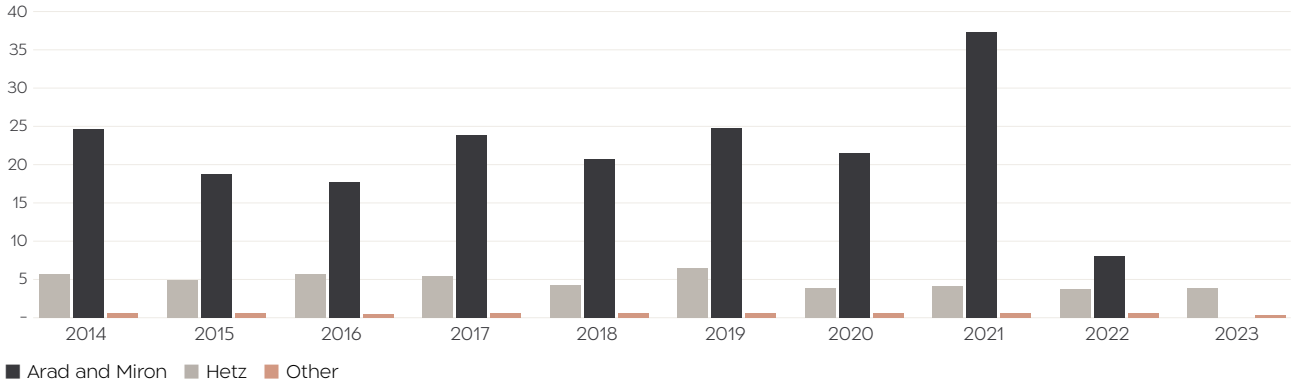
3. **Various deposits ("Emissions")** - Loans generated by historic agreements with provident funds. These loans are CPI- linked with fixed interest rates of 4.95% to 5.95%. In 2023, nearly NIS 569 million was raised in this instrument, resulting in a negative net raise of approximately NIS 297 million.

Funding Instrument	Principal Funding	Principal Redemptions	Net Funding
Pension ("Arad")	-	1,870	(1,870)
Life insurance ("Hetz")	3,978	5,482	(1,504)
Other	569	866	(297)
Total	**4,547**	**8,218**	**(3,671)**

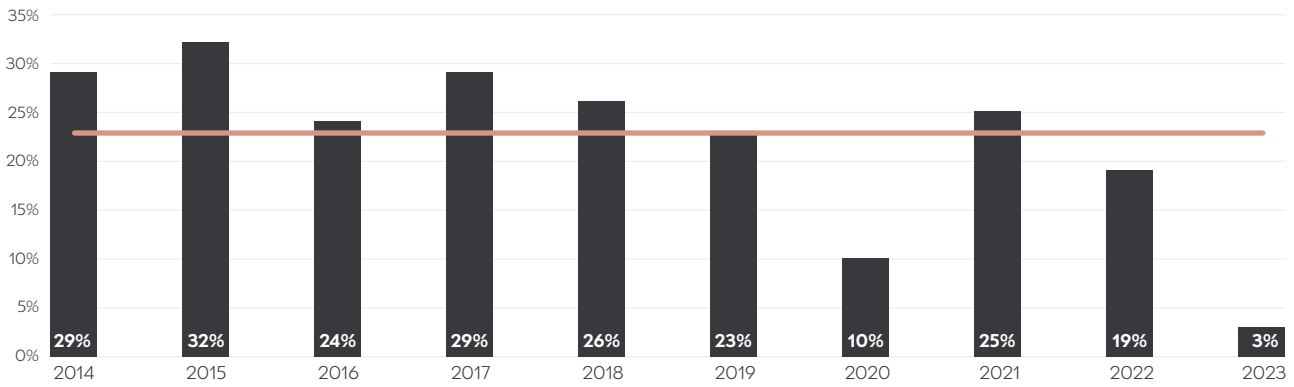
*The data in the above table is presented in NIS millions and refers to 2023

[1]The final issuance of the Arad bonds was on September 1, 2022. As of October 1, 2022, the Government Debt Management Unit ("GDMU") has granted pension funds yield guarantees in accordance with an alternative mechanism, ensuring yields on a portion of the pension portfolio similar to the previous mechanism.

Domestic Funding by Non-Tradable Debt 2014-2023 (NIS Billions)



Non-Tradable Funding, Percentage of Total Funding, 2014-2023

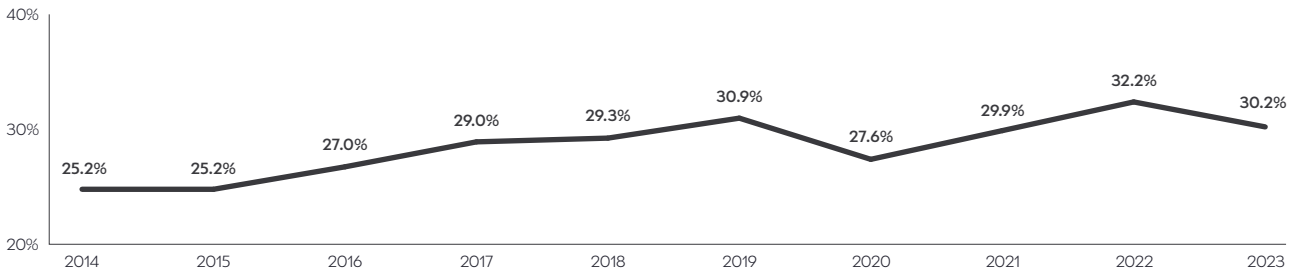


An assessment conducted by the GDMU revealed that at a steady deficit of 3%, the level of 'tolerance' (percent of non-tradable funding out of total funding, without a reduction in tradable and external financing) was 23%. With certain adjustments, it can reach 25%.

As illustrated in the chart, starting from 2014, the average non-tradable domestic funding, as a percent of total funding, was above the tolerance threshold, meaning that it could possibly reduce the tradable domestic and external financing. The exception to this was in 2020, due to the market effects of the pandemic, and 2022 due to the designated bond reform.

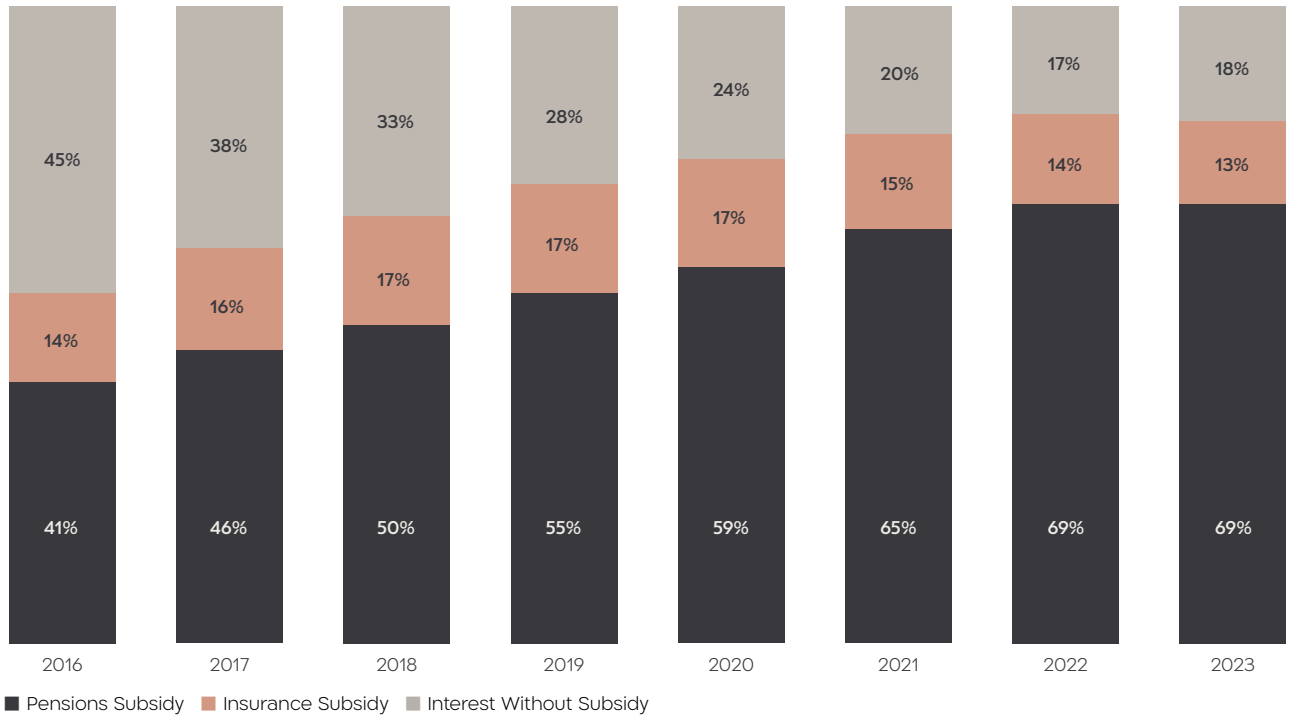
IN 2023, THE STOCK OF NON-TRADABLE DOMESTIC DEBT INCREASED BY APPROXIMATELY 2.2% TO ROUGHLY NIS 340.9 BILLION. THIS CONSTITUTES NEARLY 30.2% OF TOTAL DEBT.

Non-Tradable Stock, Percentage of Total Stock, 2014-2023



The Subsidy Cost of the Non-Tradable Debt

The following chart displays the interest payments on the non-tradable debt portfolio, relating also to the subsidized portion of the interest expenses. The subsidy reflects the difference between the interest paid on bonds according to the law or to the agreements, and the market interest rates at the time of the issuances.



If these bonds were issued as tradable bonds, the interest expenses on the non-tradable debt in 2023 would have been 18% of the actual interest payments. This means that in 2023, out of the roughly NIS 16.3 billion in interest expenditures for designated bonds, the interest payments without subsidy amounted to roughly NIS 2.9 billion.

ORGANIZATIONAL CHART GOVERNMENT DEBT UNIT



רכזת לשכת חטיבת המימון
Executive Assistant

עמית שרון Amit Sharon

אסטרטגית ראשית חטיבת המימון
Chief Strategist

חן רייכמן כהן Chen Reichman Cohen

....

אורית מלול Orit Malul

מחלקת ניהול סיכונים
Risk Management Department

דור עמית מנהלת המחלקה
Dor Amit Head of the Department

....

אדי שמש Eddie Shemesh

אופק גבריאלי Ofek Gabrieli

דוד גומרי David Gomeri

מחלקת חוב חיצוני
Global Debt & FX Transactions Department

סער אלימלך מנהל המחלקה
Saar Elimelech Head of the Department

....

ליאור אושרי Leeorr Oshrey

ויקטוריה מתייב Victoria Mataeva

מחלקת הנפקות בשוק המקומי
Domestic Primary Issuances Department

ארז גולן מנהל המחלקה
Erez Golan Head of the Department

....

ערן לפל Eran Leffel

שיר סער Shir Saar

דביר כהן Dvir Cohen

מבנה ארגוני יחידת החוב הממשלתי

גיל כהן סגן בכיר לחשב הכללי
מנהל חטיבת המימון והאשראי

Gil Cohen Senior Deputy Accountant General Head of Finance, Debt & Credit Division

יחידת החוב הממשלתי
Government Debt Management Unit

פיליפ איחלזון מנהל היחידה
Philip Yhelzon Head of the Unit

מנהל קשרי משקיעים גלובלי
Head of Investor Relations

ג'ייסון ריינין Jason Reinin

מחלקת תקבולים ותשלומים
Receipts & Payments Department

אדי טרנר מנהל המחלקה
Edi Terner Head of the Department

חנה סלע סגנית מנהל המחלקה
Hana Sela Deputy Head of the Department

....

אורנה ארד Orna Arad

גנאדי ניימן Gennady Naiman

יעל לוין Yael Levin

מחלקת חוב מקומי וניהול נזילות
Domestic Debt and Cash Management

יוסי ניסים מנהל המחלקה
Yossi Nisim Head of the Department

מחלקת מערך אמצעי ובקרת מסחר
Middle Office & Secondary Market Compliance Department

טל פלג מנהל המחלקה
Tal Peleg Head of the Department

....

אריאל קמחי Ariel Kimhi

משרדי היחידה רח' קפלן 1, ירושלים • **02-5317555** • **מייל קשרי משקיעים** debt.ir@mof.gov.il