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Israel Corporation Ltd.

Form 121

Public

Registrar Number: 520028010

Securities of the Corporation are listed in the Tel Aviv Stock Exchange

Short name: Israel Corporation

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Date of Transmission: January 27, 2016

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To:	To:
The Securities Authority	The Tel Aviv Stock Exchange
www.isa.gov.il	www.tase.co.il

Immediate Report

The Event: Maalot's Report

Attached is Maalot's report - affirmation of 'ilA+' rating and revision of rating outlook to negative due to increase in the LTV ratio and decrease in the margin on the financial covenant vis-à-vis some of the lenders.

The date when the event first became known to the corporation: January 26, 2016

Time: 18:00

The name of the authorized signatory to the report and the name of the authorized electronic signatory: Maya Alcheh-Kaplan

Position: Vice President, General Counsel and Company Secretary

Date of signing: January 27, 2016

Israel Corporation Ltd.

January 26, 2016

Research Update

'ilA+' Rating Affirmed; Outlook Revised To Negative On Increase In LTV Ratio, Decrease In Margin On Financial Covenant Vis-à-Vis Some Of Its Lenders

Primary Credit Analyst

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Research Update

‘ilA+’ Rating Affirmed; Outlook Revised To Negative On Increase In LTV Ratio, Decrease In Margin On Financial Covenant Vis-à-Vis Some Of Its Lenders

Summary

- Following a drop of about 14% in the value of the company’s investment portfolio since our last rating action, its LTV (loan to value) ratio is currently about 43%, compared to about 36% in November 2015. The current LTV ratio, which we consider an indicative metric of the company’s leverage, now exceeds the ratio we previously identified as commensurate with the current rating (below 40%).
- We assess that the company’s debt coverage ratio could weaken if deterioration occurs in the operating performance of Israel Chemicals Ltd. (“ICL”) beyond the assessment in our base-case operating scenario, against the backdrop of negative trends in financial markets in general and in commodity markets in particular.
- Due to high market volatility and the downward trend in ICL’s market capitalization, the company may violate a financial covenant vis-à-vis some of its lenders.
- We affirm Israel Corporation Ltd.’s ‘ilA+’ rating and revise its outlook to negative from stable.
- The negative outlook reflects the risk that the company’s operating performance deteriorate beyond our previous expectations, causing coverage ratios to exceed the ones we see as commensurate with the current rating, i.e. a debt to EBITDA ratio below 3.5x and an LTV ratio below 40%, as well as the risk that the company violate a financial covenant vis-à-vis some of its lenders.

Rating Action

On January 26, 2016, Standard & Poor’s affirmed its ‘ilA+’ rating on operating holding company Israel Corporation Ltd., and at the same time revised the outlook to negative from stable.

Rationale

The outlook revision to negative reflects the fact that the company’s LTV ratio now exceeds the ratio we see as commensurate with the current rating, the risk that the company violate a financial covenant vis-à-vis some of its lenders, and the risk that the company’s coverage ratios deteriorate, against the backdrop of negative trends in financial markets in general and in commodity markets in particular.

The value of the company’s investment portfolio dropped by approximately 14% since our last rating action in November 2015, mainly due to a 19% drop in the market capitalization of subsidiary Israel Chemicals Ltd. (“ICL”, BBB/Negative/ilAA/Stable). Following this drop in portfolio value, the company’s LTV ratio is currently about 43%, compared to about 36% at the time of our last rating action. The current LTV ratio exceeds the ratio we see as commensurate with the current rating, LTV below 40%. We note that following the completion of a strategic spin-off by the company of its holdings in early 2015, we have changed our methodological approach and now assess Israel Corporation's credit risks mainly through the examination of the debt coverage ratios that arise from its consolidated statements, while examining the company's LTV ratio as an indicative metric for assessing its leverage and refinancing capabilities. ICL's results are fully consolidated into Israel Corporation's financial statements, while Oil Refineries Ltd. ("Bazan", ilBBB+/Stable) is an affiliated company and its results are listed using the equity method in the affiliated companies income section.

In the base-case operating scenario in our rating update for the company published on November 23, 2015, we noted that we expect challenging conditions in the Potash market. We estimated that ICL's average selling price of potash could decline by about 10% to $280 per ton in 2016-2017, due to the ongoing supply-demand imbalance. We also estimated that, given a return to normal operation and capacity after the strike in Israeli production facilities in 2015, ICL's operating results would improve in 2016. On January 4, 2016, ICL reported signing framework agreements with customers in China to supply up to 3.4 million metric tons of potash over the next three years. The potash price for the Chinese market, an "anchor price" which largely sets supply prices in the entire potash industry, will be determined in the upcoming months in negotiations between suppliers and Chinese customers. Uncertainty in potash prices has grown, in our opinion, on the backdrop of negative trends in financial markets in general and in the commodity market in particular, and growing concerns regarding emerging market economies, especially Chinese economy, including currency depreciations that further reduces farmers' purchasing power. However, at this stage we do not find it necessary to update our base-case operating scenario, and we continue to estimate that Israel Corporation's debt to EBITDA ratio will be about 2.5x-3.0x in 2016, lower than 3.5x which is the threshold we identified as commensurate with the current rating. The negative outlook reflects the risk of deterioration in the company's debt coverage ratio if ICL's operating performance deteriorates beyond our base-case operating scenario assumptions.

Israel Corporation is currently committed to a single financial covenant vis-à-vis some of its bank lenders: net liabilities/ICL and Bazan share value (according to the agreed-upon cap on Bazan share price) of up to 60%. At the moment, this ratio is at about 49%. We believe that, due to market volatility and the downward trend in ICL's share price, about 19% since November 2015 and about 45% since the beginning of 2015, there is a larger risk that Israel Corporation violate this covenant. Such violation would be sufficient grounds for lenders to demand immediate repayment of the relevant debt.

Liquidity

Our assessment of Israel Corporation's liquidity, reflecting the analysis at the holding company level, is "adequate" according to our criteria, underpinned by material cash balances and dividend receipts from Israel Chemicals Ltd. We estimate that the ratio between the company's liquidity sources and uses will exceed 1.2x in the upcoming year. In addition, about 35% of ICL shares owned by Israel Corporation and all its Bazan shares are unencumbered, providing additional financial flexibility.

In our base case scenario we estimate that the company's liquidity sources as of January 1, 2016, are:

- Cash and tradable financial assets of about $557 million;
- Dividend receipts from subsidiaries at about $150 million-$160 million until year end 2016;
- Tax rebate of about $160 million.

Our assumptions regarding the company's uses as of January 1, 2016, are:

- Principal payment of about $300 million until year end 2016;
- Interest, general and administrative expenses of about $110 until year end 2016.
- Credit line for an affiliated company, Kenon Holdings, of up to $90 million until year end 2016 (of which, $40 million were already transferred in January 2016).

Outlook

Israel Corporation's negative outlook reflects the risk that its operating performance deteriorate beyond our previous expectations, pushing its coverage ratios to exceed those we identified as commensurate with the current rating, i.e. debt to EBITDA below 3.5x and an LTV ratio below 40%. The negative outlooks also reflects the risk of a breach of the financial covenant vis-à-vis some of the company's lenders.

Downside Scenario

We may lower the company's rating if ICL's operating performance deteriorates beyond our current assessments, causing Israel Corporation's debt to EBITDA ratio to exceed the ratio we identified as commensurate with the current rating. We believe a deterioration in ICL's operating performance may cause an additional drop in its market capitalization, thus increasing further Israel Corporation's LTV ratio. An additional decrease in the margin on Israel Corporation's financial covenant vis-à-vis some of its lenders, with no immediate action taken by the company, is also expected to lead to a downgrade. In addition, we may consider a negative rating action if ICL alters its dividend policy, which is essential for Israel Corporation's debt service.

Upside Scenario

We may change the outlook to stable if market conditions stabilize and if we expect the company's debt to EBITDA to be lower than 3.5x. We estimate that stabilization in market conditions will positively affect its LTV ratio and the margin on its financial covenant vis-à-vis some of the company's lenders.

Related Criteria And Research

- Criteria For Rating Non-Financial Corporate Issuances On Standard & Poor's Maalot's Local Rating Scale, September 22, 2014.
- Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, December 16, 2014
- National And Regional Scale Credit Ratings, September 22, 2014
- Standard & Poor's National And Regional Scale Mapping Tables, January 19, 2016
- Standard & Poor's Ratings Definitions, November 20, 2014
- Methodology: Timeliness Of Payments: Grace Periods, Guarantees, And Use Of 'D' And 'SD' Ratings, October 24, 2013
- Use of CreditWatch And Outlooks, September 14, 2009
- Corporate Methodology: Ratios And Adjustments, November 19, 2013
- Group Rating Methodology, November 19, 2013
- Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, November 13, 2012
- Methodology: Industry Risk, November 19, 2013
- Country Risk Assessment Methodology And Assumptions, November 19, 2013

- Key Credit Factors For The Commodity Chemicals Industry, November 31, 2013

Rating Details (As of 26-Jan-2016)	
Israel Corporation Ltd.	
Issuer rating	ilA+/Negative
Senior Unsecured Debt	
Series 6,7,9	ilA+
Rating history	
21-Sept-2009	ilA+/Stable
11-Feb-2009	ilAA-/Negative
30-Nov-2008	ilAA/Watch Neg
1-Jan-2007	ilAA/Stable

Standard & Poor's Maalot ratings are based on information received from the Company and from other sources that Standard & Poor's Maalot believes to be reliable. Standard & Poor's Maalot does not audit the information it receives nor does it verify the correctness or completeness of such information.

It is hereby clarified that Standard & Poor's Maalot rating does not reflect risks relating to and/or arising from breaches, through intent or oversight, of any of the obligations included in the bond documents and/or the incorrectness or inaccuracy of any of the representations contained in the documents relating to the bond offering that is the subject of this rating, Standard & Poor's Maalot report or the facts that form the basis for the opinions expressed to Standard & Poor's Maalot as a condition for the giving of the rating, fraudulent or dishonest acts of commission or omission, or any other act that contravenes the law.

The ratings could be revised as a result of changes to the information received or for other reasons. The rating should not be perceived as expressing any opinion concerning the price of the securities on the primary or secondary market. The rating should not be perceived as expressing any opinion concerning the advisability of buying, selling or holding any security.