

Shrem. Fudim, Kelner and Co. Ltd.

Part B-Directors' Report on the Company's Business Condition For the Period Ended December 31, 2005

Pursuant to the Securities Regulations (Periodic and Immediate Financial Statements"), 1970, we take pleasure in submitting to the shareholders, the Directors' Report on the Business Condition of Shrem. Fudim, Kelner and Co. Ltd.. ("the Company") for the year ended December 31, 2005 ("the reporting year" or "the reporting period"). The Company and its subsidiaries will be referred to as the Group in this report.

1. Condensed description of the entity and its business environment

The Company is a holding company that operates primarily in the areas of capital markets, industry, communications and technology, real estate and infrastructures, digital printing and commerce and services.

Capital Markets: - The Company is active in this area through its subsidiaries, Leader Capital Markets, Leader Issuances and Leader & Co. The companies provide management and underwriting services for share issuances of companies interested in raising funds from the public, management of private placements, distribution of security packages, brokerage services to investors and mainly to institutional investors, as well as investment in and trading of securities and financial instruments. In addition, the Company operates in this area through its subsidiary, Sphera Fund Management Ltd., a company which manages the Sphera Fund, a hedge fund for investments in marketable securities.

Industry: - The Company is active through Urda and the companies it controls in the field of industry and commerce, focusing on the areas of metals, component products, construction and development products, construction finishing products, paints and insulation products.

Communications and technology: - The Company is active mainly through its investee companies (direct and indirect), Shrem, Fudim, Kelner – Technologies Ltd. ("Technologies"), Telit Communications Plc, Cimatron Ltd., D.B.S. Satellite Services (1998) Ltd., Partner Communications Ltd., and Leader Tech Ltd., as well as through its direct investments.

Real Estate and Infrastructures – The Company operates through directly and indirectly held investees – Leader Real Estate, Polar Real Estate Ltd., Ofir Holdings Ltd., Sitips Ltd. ,and the holdings of the Group in additional real estate properties.

Digital Printing - The digital printing sector includes the activities of Nipson Digital Printing Systems PLC and the companies held by it.

Trade and Services – The Company operates mainly through its direct and indirect investees, Hazera (1939) Ltd., Maximedia Street Advertising Ltd., Reshet – Noga Ltd., vehicular activity in Eastern Europe, M.G.A.R – Computerized Collection Center Ltd., and Dor Chemicals Ltd.

The Company is engaged, directly and through its investee companies, in purchasing, incorporating, advancing and developing activities and companies in the aforementioned sectors. In addition, the Company is engaged in, among

other things, consulting and management services to its investee companies, hedge fund management, consulting in the field of investment banking and in consulting for and management of a number of venture capital funds.

The Company and its subsidiaries ("the Group") wish to advance and develop their existing investments while continuing to implement the business strategy they adopted, at the center of which is a business and organizational focus plan, along with the expansion of the Group's overseas activities. This strategy is intended to adapt the Group's business structure to the business environment in Israel and abroad.

The Company ended the reporting period with net income of NIS 58.5 million. This profitability constitutes a continuation of the transition to growth trends which commenced in 2004, in which the Company showed a net income of NIS 48.4 million.

The Company and the private companies under its control (excluding the impact of the results of the consolidation of the public companies Leader and Technologies) ended the years 2005 and 2004 with operating income of NIS 29.4 million and NIS 16.4 million, respectively, attributed mainly to capital market activity and to capital gains on the sale of the Company's holdings.

During the reporting period, the Company, as well as other companies of the Group, distributed cash dividends of NIS 9 million. Leader, Polar Investments and Polar Communications distributed dividends of NIS 21 million, NIS 10 million, and NIS 40 million, respectively.

Subsequent to the balance sheet date, the Company and Leader declared a cash dividend of NIS 15 million, each, while Urdan declared a dividend of NIS 10 million.

During the reporting period and until the publication of this report, the Company, Leader, and the private companies under their control sold shares and options in listed companies (mainly of Leader, DS Securities, BSR and Kamor) for an amount of NIS 202 million, and a gain of NIS 44 million.

The value of the current holdings of Polar Investments in the marketable shares of major affiliated and other companies, such as Nipson, Telit, Polar International Real Estate, Aral Communications, Partner (see paragraph 2.3.5, below), etc., totals (in proximity to the date of this report) approximately NIS 340 million and reflects an excess of value of NIS 107 million in comparison to the value of these holdings recorded in the accounts at the end of 2005.

In June 2005, the Company raised an amount of NIS 63 million as part of an issue of debentures and option warrants to the public (see Note 18(a) to the financial statements).

Subsequent to the balance sheet date, the Chairman of the Board and the CEO of the Company decided that commencing in 2006 and thereafter, the rate of the annual bonus to which they are entitled will be reduced and be equal to 5% instead of 7.5% of the representative income on which it is based, and 2% instead of 2.5%, respectively. In addition, the annual bonus will be subject to a "high-water-mark", with the calculation of the income for purposes of the annual bonus being based on an aggregate basis.

In addition, the CEO of the Company decided that commencing in 2006, the annual bonus which he is entitled to receive from Leader will be subject to a "high water mark", with the calculation of the income for purposes of the annual bonus being based on an aggregate basis – see paragraphs 2.7.5 – 2.7.6 below.

2. Exceptional events during the reporting period and until proximate to the date of circulation of this report

2.1 The Capital Market

2.1.1 The Sphera Fund ("Sphera") is a fund that invests in marketable securities, the volume of which as of the publication of this report was \$130 million. Sphera is managed by an entity controlled by the Company. During the reporting period, Leader and Polar invested an additional \$2 million and \$1 million, respectively. In addition, the Company redeemed an amount of \$1 million of its investment in Sphera.

The Sphera Fund ended the reporting period with income of NIS 100 million. The net dollar yield of the Fund during the reporting period amounted to 16.0%, compared with an increase of 21.0% in the Tel Aviv Index (in dollar terms), and an increase of 1.4% in the NASDAQ. The net dollar yield of the Fund in 2004 was 28%.

2.1.2 Subsequent to the balance sheet date, the board of directors of Leader decided to concentrate the Group's capital market activity under the banner of a new company that was incorporated on January 3, 2006, Leader Capital Markets Ltd. (Leader Capital Markets). The subsidiary of Leader was set up to hold all of the issued share capital of Leader & Co. Investment House Ltd. and of Leader Issuances (1993) Ltd., subsidiaries of Leader, which are engaged in capital market activity.

Capital market activity concentrates within it, among other things, the following activities: issuance activity, which includes provision of management and underwriting services on issuances of securities of corporations interested in raising capital from the public in Israel, management of private placements in Israel, distribution of security packages in Israel, and consulting on issuances of Israeli companies abroad; brokerage activity, which includes provision of brokerage services to investors, and mainly institutional investors; investment marketing services, as well as corporate analysis and research; and security trading activity which includes investment and trading in securities and financial instruments.

In March 2006, Leader Capital Markets raised an amount of NIS 33 million (prior to deduction of issuance costs) through an IPO on the Tel Aviv Stock Exchange.

As a result of the issuance, the share of Leader in Leader Capital Markets decreased to 66%, and it expects to record a NIS 20 million gain on the decrease in holding, in its financial statements of the first quarter of 2006 (the share of the Company is NIS 12 million). For more information, see Note 10C(2) of the financial statements.

2.1.3 On November 21, 2005, Leader Financial Asset Management (2005) Ltd., a company owned by Leader & Co. and Leader Issuances (hereinafter – "Leader Management"), entered into an agreement with Yellin-Lapidoth

Holdings Ltd. ("Yellin – Lapidoth") and its CEO, whereby Leader Management was to purchase shares of Yellin – Lapidoth. Yellin – Lapidoth is a holding company which is engaged, through its wholly-owned subsidiaries, in client investment portfolio management, and provident and education fund management, and is slated to engage also in mutual fund management. The consummation and performance of the agreement are subject to the fulfillment of certain pre-conditions one of which, as of the date of this report, has not been fulfilled. For more details, see Note 10C(2) of the financial statements.

- 2.1.4 In April 2004, a company controlled by the son-in-law of the chairman of the board of the Company (hereinafter – “Sentor”) joined the founders’ agreement of Sphera. Sentor was allotted special shares in the Fund manager and in the general partner of Sphera, which shares do not grant Sentor voting rights or the right to appoint directors, rather only equity rights.

According to the terms of the special shares, the special shares grant Sentor 5% of the equity rights commencing on April 1, 2005, an additional 5% of the equity rights will be granted to Sentor commencing on April 1, 2006, and an additional 5% of the equity rights commencing on April 1, 2007. As a result, the equity rights of the Company and the two other founders in the Fund manager and the general partner declined to 47.5%, 23.75% and 23.75% respectively in April 2005, and will be diluted to 45%, 22.5% and 22.5%, respectively on April 1, 2006, and to 42.5%, 21.25% and 21.25%, respectively, on April 1, 2007. The Company continues to hold 51% of the management shares.

The agreements between the Fund manager and the Company and among the three founders of the Fund, including Sentor (herein – the “Founders”), regulated the employment terms of the Founders as well as the equity and managerial rights and obligations of the Company and the Founders. The employment terms of each of the Founders are identical. The Founders undertook to render consulting and management services to Sphera Fund entities for a period that would not end prior to January 1, 2008.

On May 18, 2005, an extraordinary general shareholders meeting ratified the terms of the agreement with Sentor as described above. See also Note 32L of the financial statements regarding the employment of the son of the CEO of the Company.

2.2 Real estate and infrastructures

- 2.2.1 During the first quarter of 2005, Leader sold to BSR Engineering and Development Ltd., the company which exerts joint control with Leader over BSR Europe Ltd. (“BSR”), and others, all of the securities of BSR (shares, option warrants and debentures) owned by the Leader, as is, for a total amount of NIS 105 million.

In addition, upon consummation of the sale, the BSR shareholders agreement from 2002 expired, the entitlement of Leader to receive management fees from BSR expired commencing in April 2005, the right of Leader to appoint directors to the BSR board expired, and the resignations of the directors appointed by Leader to the BSR board went

into effect. Leader reported a pre-tax capital gain of NIS 29 million in the financial statements of the reporting period in respect of this transaction (the share of the Company in this income was NIS 20 million).

- 2.2.2 On November 7, 2005, Leader consummated the purchase of a piece of real estate in the Mitte area of Berlin, known as the former Postal Stagecoach Building. The purchase was made on behalf of Leader Real Estate, together with business partners and was effected through a German subsidiary, as described below.

The indirect share of Leader in the rights and income from the property is 32%, through companies set up for this purpose - SPV, as described below. The owner of the property, after consummation of the purchase described above, is a German company (the "German Company") held 20% by a private independent shareholder and by a foreign company (the "Foreign Company") through which Leader's investment was made, and which holds the balance of the shares in the German Company (80%). According to an agreement dated November 4, 2005, regarding the investment of Leader in the Foreign Company (the "Investment Agreement"), Leader will hold 40% of the capital rights and 50% of the voting rights in the Foreign Company, with the balance of the rights in the Foreign Company being held by an Austrian company held by an independent third party.

The total costs of purchasing the property, as of the date of the release of this report (including the purchase price, purchase tax, related expenses, etc.), amounted to €16.4 million. Part of the purchase of the property was financed and paid to the seller of the property through a mezzanine loan in an amount of €2 million (the "Mezzanine Loan") granted to the German Company by a limited partnership (hereinafter – the "Partnership"), the general partner of which is SFK Wing Overseas Real Estate Investments Ltd. (the "General Partner"), a subsidiary of the Company. The balance of the costs of the purchase of the property was provided to the German Company by the shareholders and paid to the seller of the property, as above, on November 7, 2005.

Leader financed the major part of its share in the purchase of the property through a loan from a financial institution, in an amount of €4 million, with the balance being self-financed.

The property purchased is a 5,700 sq.m. plot of land on which the former Postal Stagecoach Building stands, a building slated for preservation. The total built-up area is 10 thousand sq.m. In its present condition, the building is partially occupied by various tenants for rents in immaterial amounts. To the best of Leader's knowledge, the purchasers intend on positioning the Property as a luxury property and to earmark it for purposes other than the ones it currently serves. At present though, no decision has been made as to the designated purpose of the Property. To the best of Leader's knowledge, the zoning of the land is suitable to a variety of uses, including residential, commercial, and hotels.

The general partner of the partnership that provided the Mezzanine Loan is a subsidiary of the Company. The limited partners of the partnership which furnished the partnership with the funds to provide the Mezzanine Loan are unrelated parties. As part of the Mezzanine Loan, the Partnership is entitled to receive from the German Company, in addition

to interest, a percentage of the profits on the sale of the Property, should such a sale take place and under certain conditions, as stipulated in the Loan Agreement. The General Partner is entitled to a certain percentage of the profits which the Partnership is entitled to receive, as above, plus an additional commission.

- 2.2.3 On January 3, 2006, Leader, through a wholly-owned subsidiary ("Leader Real Estate"), signed a framework agreement with a third party, for the purchase of various parts of a rental apartment project in Germany. The overall project is valued at €150 million. The indirect share of Leader in the transaction is 32.5% and the investment of Leader Real Estate in the transaction is 4.5% of the total transaction.

In addition, an agreement was signed with a foreign financing institution, which is slated to place at the disposal of the transaction financing of 90% of the total transaction.

According to the agreement, the parties to the transaction were granted a period of six months to consummate their purchase of apartment properties at the abovementioned purchase price (including various purchasing expenses) of €150 million. In the first phase, immediately after the signing of the financing agreement, the parties consummated the purchase of apartment properties which include 1,500 apartment units, for a total purchase cost of €50 million (including various purchase costs).

- 2.2.4 Proximate to the date of the release of this report, Leader, through Leader Real Estate, signed a framework agreement with a third party (the "Partner") for the purchase of rental commercial properties in Germany. The total value of the transaction was €120 million. The indirect share of Leader Real Estate in the transaction is 47.5%. Leader Real Estate's share in the transaction is 4.7%.

In addition, an agreement was signed with a foreign financing institution, which is slated to place at the disposal of the transaction, financing of 90% of the total transaction. Supplementary financing of 3% of the value of the transaction will be placed at the disposal of a partnership jointly managed by the companies, one of which is controlled by the Company.

According to the agreements, the parties to the transaction were granted a period of six months to consummate their purchase of commercial properties at the abovementioned purchase price (including various purchasing expenses) of €120 million. In the first phase, immediately after the signing of the financing agreement, the parties consummated the purchase of ten commercial properties which include a mall and supermarkets, for a total purchase cost of €40 million (including various purchase costs).

- 2.2.5 In February 2006, Polar Investments signed a memorandum of understanding with Boimelgreen Capital Ltd. (hereinafter – the "Purchaser") and Polar Real Estate (hereinafter – the "Memorandum of Understanding"), for the purchase of 50% of the shares of Polar Real Estate by the Purchaser, and cooperation between Polar Investments and the Purchaser with regard to Polar Real Estate (the "Transaction").

According to the Memorandum of Understanding and the principles set out in the negotiations being conducted between the parties, the Purchaser will

purchase 50% of the share capital of Polar Real Estate in return for a payment to the Company of \$10 million and the granting of shareholders loans to Polar Real Estate, as detailed below. Upon the consummation of the Transaction, the Purchaser will pay Polar Investments an amount of \$5 million against a transfer of 10% of the shares of Polar Real Estate, with the remaining 40% of the shares being deposited in trust for the Purchaser. These shares will be released by the trustee to the Purchaser upon the payment of the entire consideration to Polar Investments and the granting of the shareholders loans to Polar Real Estate, within 18 months following the consummation of the Transaction (the "Exercise Period").

The Purchaser undertakes to place shareholders loans at the disposal of Polar Real Estate from time to time during the Exercise Period upon demand, in amounts equal to the loans of Polar Investments to Polar Real Estate, up to an amount of US\$ 32 million (the "Purchaser's Loans"). These loans will be placed by Polar Real Estate at the disposal of one of its subsidiaries (the "Designated Company") solely for use in financing new projects in Israel and abroad.

The Purchaser's Loans will bear interest at a rate of 7% per annum (preferred return), to be paid from the profits of the Designated Company.

It was agreed that upon the demand of Polar Real Estate from its shareholders to place additional financing at its disposal for the purpose of carrying out current business or business that will commence prior to the signing of a detailed agreement regarding the Transaction, Polar Investments will be solely responsible to arrange the aforementioned financing (that will be limited to an agreed-upon amount). When the Company provides the aforementioned financing, the Purchaser will provide financing to Polar Real Estate in an identical amount, for purposes of carrying out new business by Polar Real Estate.

As part of the detailed agreement to be signed regarding the Transaction, there will be, among other things, an arrangement that will enable Polar Real Estate to increase its shareholders' equity. The arrangement will set out a mechanism to accelerate the receipt of loans from the Purchaser, as well as other agreed-upon conditions, including the undertaking of Polar Investments and the Purchaser to capitalize loans in amounts of US\$ 20 million each, to the capital of Polar Real Estate under certain circumstances. There will also be an arrangement that will result in the release of Polar Investments from all of the guarantees and/or collateral that it provided to Polar real Estate. Consummation of the Transaction is contingent upon the signing of a detailed agreement by March 31, 2006 and the obtaining of certain approvals, to be set forth in the detailed agreement. In the event that the Transaction is consummated, Polar Investments does not expect it to have a material impact on the results of its operations.

- 2.2.6 In November 2005, Polar International Real Estate, together with the rest of the shareholders of a U.S. Corporation that holds the rights to purchase the residential portion of a building in Manhattan, New York (containing 690 apartments) (hereinafter – the "Corporation"), signed an agreement for the sale of all of the rights of the Corporation, for an amount of \$120 million. The closing date of the sales agreement was set for the date of the closing of the agreement to purchase the building, and consummation of the sales agreement is subject to the fulfillment of a number of conditions as detailed in the sales agreement, including

completion of the conversion of the building into apartments for sale (for more details, see Note 10C(2) of the financial statements).

- 2.2.7 Proximate to the release of this report, as part of the development of its business in additional markets around the world, Polar International Real Estate signed a memorandum of principles to set up a joint company in the U.K. that will engage in developing real estate projects. The document was signed with the following companies:

A British company engaged in the area of real estate in the U.K., with past experience in the construction of buildings that serve as centers of business, light industry, commerce, and office space. The British company will be responsible, as part of the joint company, for the construction and management of real estate projects. The British company will be entitled to receive 37% of the profits of the joint company.

An American company that will furnish up to 30% of the required shareholders' equity of the joint company and will be entitled to receive up to 24% of the profits of the joint company.

The first real estate project proposed to the joint company is property located in Hemel Hempstead, a suburb of London (the "Project"). The estimated cost of the project is \$ 23 million and the shareholders' equity to be furnished to the project by Polar International Real Estate will amount to \$ 3 million.

2.3 Communications and technology

- 2.3.1 Subsequent to the balance sheet date, the Company and Technologies decided to acquire all of the holdings of the Japanese trading company, Marubeni Corporation ("Marubeni") in Technologies, which constituted as of the date of sale, 16% of the voting rights in Technologies, for an amount of \$25 million, reflecting a share price of \$0.392 (hereinafter – the Sale of the Marubeni Shares").

As part of the Sale of the Marubeni Shares, Technologies purchased in February 2006 4,760,000 ordinary shares, par value NIS 0.01 each, of Technologies, for an amount of \$1.9 million (NIS 8.8 million). This purchase was done as part of the balance (which amounted to NIS 8.9 million prior to the purchase) available for self purchase, in accordance with the decision of the Tel Aviv District Court which approved a permissible distribution of up to NIS 10 million.

The shares purchased by Technologies became treasury shares. The Company acquired the remainder of the Technologies shares owned by Marubeni, i.e., 1,617,494 ordinary shares, par value NIS 0.01 each, for an amount of \$0.6 million (NIS 3 million).

As a result of the purchase, the Company's share in Technologies increased to 76% of the voting rights in the company.

The Sale of the Marubeni Shares was approved by the general shareholders meeting of Technologies on February 15, 2006. Upon the consummation of the Sale of the Marubeni Shares, all of the rights granted to Marubeni under the agreement dated March 2002 expired, including the rights relating to shares, the right to appoint a director on

behalf of Marubeni and the commitment of Technologies to distribute dividends.

- 2.3.2 During the last quarter of 2005, Technologies adopted a new strategy whereby it would vary and expand its investment activity, so that commencing in 2006, Technologies would engage in a new field of activity – Private Equity. This activity will include mainly investments in entities active in various fields, but the one major feature that is characteristic of all of the companies is that they all suffer from financial or operational problems or some other special circumstances that cause them to be undervalued. In the opinion of Technologies, these companies have potential for high growth or good chances of recovery that will enable them to be sold at a later date for a good return on investment.

The fund will be managed by managers on behalf of Technologies and Messrs. Doron Steiger and Ofer Yarkoni. Technologies intends on raising a total amount of NIS 120 million for the Private Equity Fund ("PE Fund") which will be raised from Technologies funds as follows: NIS 18 million will be raised through a private placement (see Note 10D(1)h of the financial statements) of convertible debentures and options to companies owned and controlled by Messrs. Doron Steiger, Ofer Yarkoni, and Nir Terlovsky (the "Investors"), NIS 32 million will be raised from the funds of a public offering and/or the Company's current funds, and the balance will be raised from external investors.

The general partner of the fund will be a partnership to be held 50% by Technologies and 50% by Messrs. Yarkoni and Steiger through a company under their control (25% will be held by Yarkoni and 25% by Steiger). The PE Fund will enter into a management agreement with a management company owned in a manner identical with the ownership of the general partner (the "Management Company"). The management organs of the general partner and the management company will be comprised of four members, two of which will be appointed by the Company and two by Yarkoni and Steiger. Decisions of these organs will be passed only by unanimous vote.

Technologies entered into agreements with Superior Cables Ltd. ("Superior"), a public company whose shares are traded on the Tel Aviv Stock Exchange, the Alpine Group, the controlling shareholders of Superior, and subsidiaries of The Alpine Group Inc. (the "Alpine Group"), regarding an investment of the PE Fund in shares of Superior. For more information, see Note 10D(2)(q) of the financial statements.

On October 10, 2005, Dr. Yehoshua (Shuky) Gleitman ("Gleitman") announced his resignation from the management of Technologies. Based on the agreement reached between Technologies and Gleitman, Gleitman will continue to manage, through a company under his control, the technological activity of Technologies which includes, among other things, the Platinum Fund and Danbar Technologies Ltd. Gleitman's resignation went into effect on November 15, 2005. Mr. Yitzchak Shrem, chairman of the Technologies' board of directors, was appointed as CEO of Technologies, immediately following approval of the general shareholders meeting of Technologies.

On October 10, Technologies Management approved the sale of 10% of its holdings in Persay Ltd. and Capital – Point Ltd. to Gleitman.

- 2.3.4 The founding agreement of the Pitango II Fund grants investors in Pitango II and concurrent investors the right to receive a refund of the success fees distributed to the fund manager if the relative profits of Pitango II are lower than the relative rate of distribution, whereby the profits were distributed to the fund manager during the life of the fund (a "claw-back"). Entitlement to these refunds may result from the distribution of profits and success fees prior to the final calculation of the amount due to the fund manager in respect of participation in earnings, for example, as a result of a distribution of earnings which was effected prior to the call for the full amount of the commitment of the limited partners. Concurrently, as part of the relationship between DS Polaris Ltd. ("DSP") and DS Polaris Consultants Ltd. ("DPC") (subsidiaries of Technologies), DSP undertook to indemnify DPC if a demand is made of the latter to refund to investors in Pitango II part of the success fees it received in the past. During 2000 and 2001, DSP recorded revenues from success fees in a total amount of NIS 56.4 million. During 2003, DPS realized that there are good chances that it will be asked to indemnify DPC for an amount of NIS 2 million in respect of success fees it received in the past. Accordingly, DSP included a provision for this amount in its 2003 financial statements.

The Company's financial statements were restated in order to retroactively reflect the correction in respect of a remeasurement of the provision in respect of the obligation to refund the success fees (the claw-back), on the basis of the maximum exposure of that obligation which derived from the founding agreements of the Pitango II Fund, in accordance with the restatement made by Technologies in its accounting records.

The maximum exposure is based on the assumption that the balance of the assets managed by the Pitango II Fund will be realized at their book value. The total exposure of DSP as of December 31, 2005 amounted to \$2.7 million (NIS 12.5 million), with NIS 2 million of this amount being recorded in the DPC financial statements of 2003, NIS 9.4 million recorded in the 2004 financial statements, and the balance of NIS 1.1 being recorded in the 2005 financial statements. The net share of the Company in these expenses in 2004 and 2005 amounted to NIS 2.1 million and NIS 0.1 million, respectively. (See Note 10D(2)(a) of the financial statements.)

- 2.3.5 In April 2005, Polar Communications consummated the sale of 3.4 million shares of Partner, out of the 4.2 million of Partner shares that it owned, at a price of NIS 32.22 per share, for total proceeds of NIS 110 million. As a result of the sale, Polar Investments recorded a pre-tax gain of NIS 95 million in the second quarter (the share of the Company was NIS 30 million).

In March 2006, Polar Communications sold its entire holdings in the share capital of Partner for an amount of NIS 25 million, to Elron Electronics Industry Ltd. Accordingly, in the first quarter of 2006, Polar

Investments will record a pre-tax gain of NIS 19.5 million (the share of the Company is NIS 5.5 million).

- 2.3.6 In April 2005, Telit announced consummation of the issue of its shares on the London AIM market, in which it raised an amount of \$44 million. As a result of the issue, the share of Polar Investments in the share capital of Telit declined to 53%. The financial statements of Polar Investments for the reporting period included a gain on the issue to a third party in an amount of NIS 79 million (the share of the Company was NIS 25 million). In September 2005, Polar Investments sold 1% of the Telit shares for an amount of NIS 4 million, so that proximate to the date of this report, Polar Investments holds 52% of the share capital of Telit.
- 2.3.7 On September 28, 2005, an allotment agreement was signed between Leader, Leader Tech (in which Leader held a 66.5% share as of the date of the agreement) and KMG Realty LLC (the "Offeree"), a company controlled by Mr. Arye Kotler ("Kotler").

The allotment agreement stipulated that further to Leader Tech's desire to vary the composition of its investments and to move into new areas of activity, it wants to sell off its venture capital portfolio. On November 1, 2005, the agreement was consummated. The agreement includes, among other things, the following: an allotment of shares to the Offeree by Leader Tech, further to which the share of Leader in Leader Tech decreased to 47%, the commitment of the Offeree to purchase, in no later than four years, additional shares of Leader Tech, the cancellation of the existing management agreements in Leader Tech, etc.

For more information pertaining to the terms of the aforementioned agreements, including the terms of the new management agreements with the Offeree and Leader Tech, see Note 10C(2)(c) of the financial statements.

- 2.3.8 Tenne is a fund for investment in Kibbutz industries, which raised an amount of \$24 million. The Company and companies under its control undertook to invest amounts of \$0.5 million and \$2.5 million in Tenne. During the period of the report, the Company and the companies it controls invested amounts of NIS 0.3 million and NIS 1.8 million, respectively. In addition, Leader holds 3% of the general partner of the Fund. Subsequent to the reporting period, the Company and companies it controls invested in Tenne additional amounts of NIS 0.5 million and NIS 2.8 million, respectively.

2.4 Trade and services

- 2.4.1 In the first quarter of 2005, Leader sold off its entire holdings in Kamor for an amount of NIS 29 million. The impact of this sale on the Company's results of operations for the first quarter is immaterial.
- 2.4.2 In August 2005, Leader entered into an agreement for the sale of its entire holdings (20%) in the shares of Agam Leaderim Holdings (2001) Ltd. for an amount of NIS 8.2 million.

As a result of the sale, Leader recorded a pre-tax gain of NIS 3 million in its financial statements for the third quarter of 2005 (the share of the Company was NIS 2 million).

- 2.4.3 In April 2005, Reshet, a company in which Polar Investments has a 36% share (indirect), won a tender for the operation of commercial television broadcasts on Channel 2, for a ten year period commencing on November 1, 2005.

In January 2006, Polar Communications, through a wholly-owned subsidiary, signed an agreement (the "Agreement") with a third party for the sale of 6% of the share capital and voting rights in Reshet, for an amount of \$ 1.8 million. The third party is also purchasing an additional 14% of the shares of Reshet from one of the other shareholders in Reshet.

Consummation of the transaction is contingent upon, among other things, obtaining the approval of the Council of the Second Radio and Television Authority, in accordance with clause 36 of the Second Radio and Television Authority Law - 1990, and fulfillment of other conditions set forth in the agreement. In the event that the transaction is consummated, as above, Polar Communications will indirectly hold 30% of the share capital and voting rights in Reshet. As a result, Polar Communications expects to record a pre-tax gain in an amount of NIS 4.5 million (the share of the Company is NIS 1.3 million).

- 2.4.4 In May 2005, an agreement was signed with Orek Ltd. (which at that time held 50% of Maximedia; "Orek") whereby Orek provided funding to Maximedia in an amount of NIS 1.5 million. Subsequently, Polar Communications acquired Orek's entire holdings in Maximedia for no consideration. As a result, Maximedia became a wholly-owned subsidiary of PolarCommunications.

In November 2005, Polar Communications signed an agreement (the "Agreement"), the consummation date of which was in December 2005, with News Out of Home BV (the "Purchaser") regarding the sale of part of Polar Communications' holdings in Maximedia. Under the Agreement, the purchaser purchased from Polar Communications 67% of the share capital of Maximedia for an amount of \$4 million (of which an amount of \$690 thousand was paid to Maximedia and the balance to Polar Communications). In addition, the agreement set out a number of arrangements between Polar Communications and the Purchaser, as detailed in Note 10C(2) of the financial statements.

As a result of the sale, Polar Communications recorded a pre-tax gain of NIS 29 million (the share of the Company is NIS 8 million) (after the share of Polar Communications in the expenses of Maximedia in the fourth quarter of 2005, in an amount of NIS 5 million).

2.5 Industry

- 2.5.1 On March 10, 2005, Urdan signed agreements with a third party which is not an interested party in Urdan and in which Urdan is not an interested party (the "Purchaser"), whereby Urdan would sell the Purchaser its rights in a 56 dunam (gross) plot of land and the buildings constructed

thereon, in the old industrial zone in Netanya (the "Property"), upon which Urdan's foundry is located (the "Plant"), for an amount of \$13 million. Urdan will lease the property from the purchaser for a period of 10 years, for an amount of \$1.3 million per annum. The leasing fees for the first year were paid by Urdan in advance, upon the consummation of the transaction in August, as described below.

In August 2005, Urdan completed the aforementioned transaction and as a result, Urdan included in its financial statements for the third quarter of 2005 a net capital gain (after tax) of NIS 27 million. As a result of this transaction, the Company reported a pre-tax profit in an amount of NIS 4.4 million in its financial statements for the third quarter of 2005, reflecting its share in Urdan's pre-tax profit on this transaction, after allocation of excess cost. See Note 22A(3) of the financial statements.

- 2.5.2 In November 2005, Urdan, through its subsidiary, Urdan Rakam (Armored Fighting Vehicle) Ltd. (hereinafter – "Urdan Rakam"), a wholly-owned subsidiary of Urdan, entered into an agreement with the Israel Military Industries Ltd. (hereinafter – "TAAS", the "Urdan Rakam Agreement"), whereby Urdan Rakam would supply 173 suspension units and related services, as part of the betterment project of the M-60 tank carried out by TAAS for the Turkish army (the "Turkish Customer").

The amount of the Urdan Rakan Agreement is \$26.2 million and the major supply times will be for a two year period, commencing in the fourth quarter of 2006.

As part of the performance of the Urdan Rakam Agreement, Urdan Rakam entered into an agreement in November 2005 with Ashot Ashkelon Industries Ltd., a subsidiary of TAAS undergoing privatization, for the supply of significant components by Ashot Ashkelon to be included in the aforementioned suspension units. The amount of the Ashot Ashkelon Agreement is \$7 million, with major supply times for a two year period, commencing in the fourth quarter of 2006.

In addition, in November 2005, Orlite Industries (Millennium 2000) Ltd. ("Orlite Millennium"), a wholly-owned subsidiary of Urdan (indirectly), also entered into another agreement with TAAS, whereby Orlite Millennium will supply TAAS with ammunition boxes for the tanks as part of the Turkish project. The amount of the Millennium Agreement was \$9.5 million, with major supply times for a two and a half year period, commencing in the third quarter of 2006.

The payments by TAAS to Urdan Rakam (and concurrently to Ashot) and to Orlite Millennium are contingent upon, among other things, the receipt by TAAS of concurrent payments from the Turkish customer, some of which are significant advances (against which Urdan Rakam, Ashot and Orlite Millennium have to provide bank guarantees) and the rest of which will be paid out in accordance with the progress of the Turkish Project.

- 2.5.3 In March 2005, the Israel Electric Company Ltd. announced that the agreement between it and Orlite Industries (Millennium 2000) Ltd.

would be extended for another year, until the end of May 2006, in accordance with the option granted to it as part of the agreement that was signed in the past for the supply of electricity distribution cabinets by Orlite Millennium. See also Note 22A(3) of the financial statements.

- 2.5.4 In the second quarter of 2005, E.E.R. Environment and Energy Resources Company (Israel) Ltd. ("E.E.R.", an affiliated company), signed a memorandum of understanding for cooperation outside of the U.S. with Duratek Services Inc. ("Duratek"), a company whose parent company is traded on the NASDAQ and which is engaged in the destruction of radioactive wastes. The goal of the cooperation is management of projects for the handling of radioactive waste, utilizing the technological platforms of E.E.R. and the engineering and operational expertise of Duratek.

The memorandum of understanding does not contain any financial conditions in connection with the development or the performance of the projects. Such conditions will be set out in negotiations between the parties when submitting a joint proposal for a project. Concurrently, another memorandum of understanding was signed whereby it was agreed to cooperate on a project in Chernobyl (see below).

In June 2004, E.E.R. signed a memorandum of principles to cooperate with the Ukrainian government and the Korchtov Institute, whereby the Ukrainian government will use technology that was jointly developed by the Korchtov Institute, the Radon Institute and E.E.R., for the construction in Chernobyl of a number of installations for the destruction of low-radiation radioactive wastes (the "Project").

In August 2005, the Ukrainian government ratified the memorandum of principles, and E.E.R. will serve as the head contractor of the Project. E.E.R. submitted the feasibility documents for the Project to the Ukrainian government, in advance of the signing of a detailed agreement. As of the date of the preparation of this report, a detailed agreement has not yet been signed between the parties and a plan for the financing of the project has not yet been formulated.

In the third quarter of 2005, E.E.R. signed agreements for the raising of up to \$4.5 million from a number of the existing shareholders of E.E.R. (the "Investors"). The fundraising will take the form of shareholders' loans (the "Shareholders' Loans"), together with the granting of options to the Investors for no consideration (the "Option Warrants"). The Option Warrants are exercisable into shares of E.E.R. (in whole or in part) for a total exercise price of \$4.5 million, during a five year period and at an E.E.R. company value of \$80 million (pre-money) – similar to the value of the previous fundraising done in E.E.R. and subject to a number of adjustments (e.g., distribution of a dividend, bonus shares, etc.).

The Shareholders' loans will be repaid out of E.E.R.'s cash balance, as to be determined by the board of directors of E.E.R. In addition, it was stipulated that in the event of an additional fundraising round done by E.E.R., in an amount of \$7.5 million, the shareholders' loans will be repaid. In the event that any of the Investors do not provide all or part of

their shares of the aforementioned fundraising, their rights will lapse in respect of that portion of the funds not provided and/or that will not be provided in the future, and the other Investors, who did provide their shares, will be entitled to invest in their stead.

As part of the Investors who are participating in this fundraising, which investors are existing shareholders of E.E.R, Urdan will participate in an amount of \$950 thousand, and the Company and Technologies will participate in amounts of \$400 thousand and \$150 thousand, respectively. Funds managed by the Company will also participate in an amount of \$190 thousand.

In the event that the Company exercises the options granted to the Company, Urdan and Technologies in accordance with its investment, as above, the options will grant the Company, Urdan and Technologies, together with the shares of E.E.R held by them at present, 7.1%, 16.4% and 2.9% respectively of the share capital of E.E.R, under a full dilution assumption (i.e., under the assumption that all existing convertible securities will be converted into E.E.R. shares and under the assumption that all of the options from the abovementioned fundraising are also exercised).

In addition, in the last two months, negotiations have been conducted in connection with a possible investment of \$10 million in the share capital of E.E.R. by a strategic investor. The negotiations were terminated in March 2006 due to disputes in connection with the terms of the investment.

2.6 Digital Printing

2.6.1 In March 2005, as part of another issuance of shares on the AIM market in London, Nipson raised an amount of \$11 million. In addition to and as part of the issuance, Polar Communications sold (directly and indirectly) shares of Nipson for an amount of \$10 million. Upon completion of the issuance and the sale, the (indirect) share of Polar Communications in the share capital of Nipson declined to 50.7%. The financial statements of Polar Investments included a pre-tax gain of NIS 39 million on the issuance and sale to a third party (the share of the Company was NIS 13 million).

2.7 Other events

2.7.1 For information pertaining to private placements and issuances made by the Company and its subsidiaries through prospectuses during the reporting period and other events, see Part A – Description of the Business of the Corporation attached to this periodic report.

2.7.2 On November 3, 2005, the board of directors of Leader approved a self purchase of Company shares in a total amount of NIS 10 million and authorized Company Management to make the purchases.

2.7.3 On November 24, 2005, the board of directors of the Company ratified and approved a self purchase of Company shares on the stock exchange, from time to time, in a total amount not to exceed NIS 10 million

(including shares already purchased during 2005) and authorized Company Management to make the purchases.

2.7.4 Mr. Yitzchak Shrem, Chairman of the Board, renders management services to the Company through a company under his control (the "Shrem Company"). Under the agreement with the Shrem Company, it is entitled to receive an annual bonus on the basis of the pre-tax adjusted income (consolidated), plus the share of the Company in the results of affiliated companies (the "Representative Income"). The Shrem Company gave notice as follows:

- A. Commencing in 2006 and thereafter, it agrees that the rate of the annual bonus will be reduced to 5% (instead of 7.5%) of the Representative Income.
- B. In addition, the annual bonus will be subject to a high-water mark, with the calculation of the income for purposes of the annual bonus being based on an aggregate basis. In the event that in any given year, commencing in 2006 and thereafter, the Company ends the year with a loss, the amount of the loss will be deducted from the Representative Income to be earned by the Company in the years following the year in which it incurred the loss. See also Note 32B of the financial statements.

2.7.5 Mr. Yair Fudim, Director and CEO of the Company, provides the Company with management services through a company under his control ("Fudim Co."). According to the agreement with Fudim Co., it is entitled to receive an annual bonus, computed on the basis of the pre-tax adjusted income (consolidated), plus the share of the Company in the results of affiliated companies (the "Representative Income"). Fudim Co. notified the Company that:

- A. Commencing in 2006 and thereafter, it agrees that the rate of the annual bonus will be reduced to 2% (instead of 2.5%) of the Representative Income.
- B. The annual bonus will be subject to a "high-water mark", with the calculation of the income for purposes of the annual bonus being based on an aggregate basis. In the event that in any given year, commencing in 2006 and thereafter, the Company ends the year with a loss, the amount of the loss will be deducted from the Representative Income to be earned by the Company in the years following the year in which it incurred the loss.

In addition, Mr. Yair Fudim, Chairman of the Board, Director and CEO of Leader, provides Leader with management services through a company under his control ("Fudim Co."). According to the agreement with Fudim Co., it is entitled to receive an annual bonus, computed on the basis of the pre-tax adjusted income (consolidated), plus the share of Leader in the results of affiliated companies (the "Representative Income").

Fudim Co. notified Leader that, commencing in 2006 and thereafter, the annual bonus will be subject to a "high-water mark", with the calculation of the income for purposes of the annual bonus being based on an aggregate

basis. In the event that in any given year, commencing in 2006 and thereafter, Leader ends the year with a loss, the amount of the loss will be deducted from the Representative Income to be earned by Leader in the years following the year in which it incurred the loss. See also Note 32C of the financial statements.

3. Financial condition

The following table presents data from the consolidated balance sheet and from the balance sheet of the Company and the private companies under its control (*) in reported NIS millions of December 2005:

	As of December 31, 2005			As of December 31, 2004
	Consolidated balance sheet	Company balance sheet	Balance sheet of Company and controlled private companies (*)	Balance sheet of Company and controlled private companies (*)
Current assets	2,141.7	133.4	145.7	90.8
Investments in companies and loans to affiliated and other companies	736.5	331.5	296.7	299.3
Real property	634.1	-	-	-
Fixed assets	646.6	23.7	25.2	26.0
Other assets and deferred charges	135.4	2.1	4.1	1.8
Total assets	<u>4,294.3</u>	<u>490.7</u>	<u>471.7</u>	<u>417.9</u>
Current liabilities	1,488.7	77.8	85.3	125.7
Long-term liabilities	1,793.5	134.6	102.1	62.8
Minority interest	717.8	-	6.0	5.6
Debentures convertible in shares of the Company	11.7	11.7	11.7	-
Receipts in respect of options issued by subsidiaries	16.0	-	-	-
Shareholders' equity	<u>266.6</u>	<u>266.6</u>	<u>266.6</u>	<u>223.8</u>
Total liabilities and shareholders' equity	<u>4,294.3</u>	<u>490.7</u>	<u>471.7</u>	<u>417.9</u>

(*) In this report, the meaning of "the Company and the private companies under its control" is the consolidated balance sheet in which public companies owned directly by the Company are presented on the equity method (Leader and Shrem, Fudim, Kelner-Technologies Ltd. ("Technologies")).

- The Company's shareholders' equity as of December 31, 2005 amounted to NIS 266.6 and represented approximately 54% of total assets of the Company and the private companies under its control. Shareholders' equity as of December 31, 2004 totaled NIS 223.8 million and represented approximately 54% of total assets.
- The increase in shareholders' equity in the reporting period derives mainly from the Company's earnings of NIS 58.5 million, less the NIS 9.2 million dividend paid by the Company.
- Current assets amounted to NIS 147.5 million as of December 31, 2005 as compared to NIS 90.8 million at the end of 2004. The increase in current assets is primarily the result of an increase in cash due to the sale of the shares of Leader and an increase in the volume of the portfolio of marketable securities due to the profits of the Sphera Fund.
- Investments and loans in investee and other companies amounted to approximately NIS 296.7 million as of the end of December 2005 similar in amount to the NIS 299.3 million at the end of December 2004. The Company's share in the earnings of investee companies (mainly Leader) during the reporting period amounted to NIS 46.9 million, after deducting the effect of the realization of DS Securities, as described above.
- The financial liabilities of the Company and the private companies under its control, less their liquid resources, amounted to NIS 53 million as of the reporting date, compared with NIS 98 million as of December 31, 2004, reflecting the continuing trend in the improvement of liquidity and the decrease in the liabilities of the Company.

4. Operating results of the Company and the private companies under its control

General

As stated above, the improvement in the capital markets, the efficiency measures taken by the Company and the focusing of the Group's business strategy all made their mark on the continued improvement of the Group's results of operations and the growth trend.

The Company ended the year with income of NIS 58.5 million, compared with NIS 48.4 million in 2004. The increase in income during the reporting year derived mainly from an increase in revenues, as described above, and mainly from the share of the Company in the results of investee companies (primarily Leader).

As part of the Company's policy of reorganizing its capital structure and reducing its financial liabilities, the Company issued long-term debentures and option warrants during the reporting period, for total gross proceeds of NIS 74 million, most of which was used to reduce short-term credit.

The following table presents data from the statements of operations of the Company and the private companies under its control (*) in reported NIS millions of December 2005:

	2005	2004	2003
Revenues from consultation, management, and participation in the earnings of funds	45.0	39.3	18.9
Profit (loss) from long-term investments, net	7.4	(1.6)	1.4
Profit from marketable securities, net	16.6	14.7	34.7
Total costs and other Expenses	<u>(39.6)</u>	<u>(36.0)</u>	<u>(39.0)</u>
Net income before financing	29.4	16.4	16.0
Financing expenses, net	<u>(10.6)</u>	<u>(11.3)</u>	<u>(14.4)</u>
Profit after financing expenses	18.8	5.1	1.6
Profit from decline in percentage held	1.2	4.0	6.2
Company's share in profits (losses) of investees, net	49.1	(**)46.9	(38.5)
Tax expense	(0.8)	(0.5)	(2.2)
Minority interest in Profits of subsidiaries	<u>(9.8)</u>	<u>(7.1)</u>	<u>-</u>
Net income (loss) for the Period	<u>58.5</u>	<u>(**)48.4</u>	<u>(32.9)</u>

(*) In this report, the meaning of “the Company and the private companies under its control” is the consolidated statement of operations in which public companies held directly by the Company are presented on the equity method (Leader and Technologies).

(**) The financial statements were restated to retroactively reflect a correction in respect of the remeasurement of the provision for the obligation to refund success fees (claw-back), on the basis of the maximum exposure of that obligation, which derived from the agreements that set up the Pitango II fund, operated by a subsidiary of Technologies.

The operating results of the Company and the private companies under its control during the reporting period are explained as follows:

- The Company and the private companies under its control presented turnover from consulting, management and participation in the profits of funds in 2005 in an amount of NIS 45 million, compared with NIS 39.3 million in 2004.

The increase in turnover during the reporting period is the result of an increase in the share of the Company in management fees and participation in the profits of the Sphera Fund, due to, among other things, an increase in the turnover of the Sphera Fund and from income from the participation of the Company in the profits of funds.

- During the reporting period, the Company presented profits from marketable securities of NIS 16.6 million as compared with NIS 14.7

million in 2004 (including profits on marketable securities from the Sphera Fund).

- The Company's share in the earnings of investee companies amounted to NIS 49.1 million in the reporting period, compared with NIS 46.9 million in 2004.
- Total costs and expenses amounted to NIS 39.6 million in 2005, compared with NIS 36.0 million for 2004 (NIS 7.9 million in the fourth quarter, compared with NIS 11.7 million in the same quarter last year). The net increase in the costs of the reporting period was due mainly to the increase in the provision for bonuses to executives and employees as a derivative of the performances of the Company and privately held investees and the consolidated results of operations, partially set off by the refund of expenses in respect of litigation which was received during the first quarter of the year (in the same period last year, the Company bore expenses in respect of that litigation).
- The financing expenses of the Company and the private companies under its control amounted to approximately NIS 10.6 million in the reporting period (NIS 2.7 million in the fourth quarter) as opposed to NIS 11.3 million in 2004 (NIS 2.5 million in the fourth quarter of 2004). The financing expenses remained stable, notwithstanding the decrease in the liabilities of the Company, due to the negative impact of the increase in the "known" CPI during the year (2.7%) and due to the strengthening of the U.S. dollar versus the shekel (6.7%) over last year.

5. Consolidated operating results of the Company

Revenues from sales, services, consultation, management and underwriting totaled approximately NIS 1,903.5 million for the reporting year as compared with revenues from sales and services of NIS 1,814.0 million for 2004 and NIS 1,368.3 million in 2003. The increase in revenues from sales and services in the reporting period resulted mainly from the growth in revenues of Telit, from the initial consolidation of the operations of Maximedia, the increase in sales of the industrial segment, mainly in the area of paints and insulation material, and the consistent increase in the turnover of the capital market, as described above.

The profit from investments in investee and other companies and in net assets. for the reporting period amounted to approximately NIS 357.2 million as compared to a profit of NIS 159.0 million in 2004 and a loss of NIS 1.4 million in 2003. The profit for the reporting period is primarily the result of an issue to a third party and the sale of the shares of Nipson, from the issue of Telit shares to a third party and the realization of investments in marketable and other companies, such as Partner, BSR, Urdan, Agam, DS Securities, etc.

The improvement in revenues as well as the capital gains in 2005 resulted in pre-tax earnings for the reporting year of approximately NIS 208.3 million, compared with NIS 123.1 in 2004 and a loss of NIS 75.9 million in 2003.

The following table summarizes the operating data from the consolidated financial statements (in reported NIS millions):

	2005	2004	2003
Revenues from sales, services, consultation management and underwriting	1,903.5	1,814.0	1,368.3
Gain (loss) from long-term investments, assets, etc., net	357.2	159.0	(1.4)
Gain from marketable securities, net	66.8	44.6	110.5
Company's share in earnings of investees, net	-	37.7	10.9
Total revenues	2,327.5	2,055.3	1,488.3
Costs of sales and services	1,464.8	1,365.9	999.2
Selling and marketing	202.7	173.8	159.4
General and administrative	268.8	251.6	228.0
Share of Company in losses of investees, net	21.9	-	-
Financing, net	161.0	140.9	177.6
Total expenses	2,119.2	1,932.2	1,564.2
Profit (loss) before taxes on Income	208.3	123.1	(75.9)
Taxes on income	68.0	16.5	16.3
Profit (loss) after taxes on income	140.3	106.6	(92.2)
Minority interest in losses (gains) of subsidiaries, net	(81.8)	(58.2)	69.0
Loss attributed to discontinued operation	-	-	(9.7)
Net profit (loss) for the year	58.5	48.4	(32.9)

See Note 30 to the financial statements for data on operating segments.

6. **Directors with accounting and financial expertise**

The Company believes that the experience, education, and qualifications of the members of the board of directors provide them with the proper tools to meet the obligations of the board of directors in connection with the financial statements of the Company. Therefore, the Company determined that the minimum number of directors having accounting and financial expertise to be two directors, taking into consideration, inter alia, the size of the Company, the type and complexity of its operations, the number of members of the board of directors and the composition of the board of directors which includes members having management and professional experience and qualifications.

The members of the board of directors who are, in the estimation of the Company and to the best of its knowledge, directors with accounting and financial expertise, and the information that serves as support for this determination are as follows:

Itschak Shrem, Chairman of the Board - academic education in the areas of economics and business administration. He has been serving for many years as Chairman of the Board and Deputy Chairman of the Board of public companies and as a director of many companies, including public companies. Mr. Shrem has experience and knowledge that he has accumulated in all matters that are characteristic of the capital market, to investment banking and to the remaining sectors in which the Company operates, and he is also directly responsible for the approval and issuance of the financial statements.

Yair Fudim, CEO and Director - academic education in the areas of economics and business administration. He has been serving for many years as CEO of public companies and as a director of many companies, including public companies. Mr. Fudim has experience and knowledge that he has accumulated in all matters that are characteristic of the capital market, to underwriting and to the remaining sectors in which the Company operates, and he is also directly responsible for the approval and issuance of the financial statements.

Rubin Zimmerman, Deputy Chairman of the Board - has broad experience in business management and serves as a director in public companies.

Avraham Podohzer, Avner Cohen and David Leviatan-each has served for many years as a director and CEO of companies, and in this framework, have accumulated knowledge and experience in matters related to the capital market.

Vered Reichman-academic education in the areas of economics and business administration. She has served for many years as a CEO and serves as director in various companies, including a bank and economic institutions. She has vast knowledge and experience in business management and financial management.

7. **Transactions from operations in the derivatives market**

In the period of the report, Urdan executed a number of forward transactions to partially hedge against the exposure to changes in the exchange rate of the dollar in respect of the proceeds of the sale of Urdan's property rights in Netanya as described above. These transactions were closed in August 2005 at a loss of NIS 0.2 million which was deducted from the gain on the sale of the property rights in Netanya.

The maximum holding of Urdan in derivatives during the period of the report was in the aforementioned forward transaction and was a sale of \$6 million.

In addition, as of the balance sheet date, a subsidiary of Urdan, Aloni, has "call" options for the purchase of dollars against shekels as follows: \$2.25 million at exercise prices ranging between NIS 4.74 and 4.78 per dollar, with a fair value of an asset of NIS 11 thousand.

These transactions are for the period until March 31, 2006. The maximum holding of the Aloni in derivatives was a CALL option on \$3.0 million and €1.5 million. The maximum sale of Aloni in derivatives was a PUT option on \$5.7 million and €1.5 million. The maximum holding of Aloni in

these derivatives was on March 31, 2005. The aforementioned transactions were intended for hedging against the exposure in the area of foreign currency supplier credit.

In addition, the maximum holding of another subsidiary of Urdan, Univerkal, in derivatives for hedging purposes was in a forward transaction for the purchase of foreign currency (mainly the dollar) and amounted during the reporting period to NIS 12.4 million, in January 2005. As of the balance sheet date, there were no derivative transactions made by Univerkal.

As of December 31, 2005, Polar Investments has a Call option for the purchase of dollars against the euro as follows: €20 million at an exercise price of \$1.2 per euro, with a fair value of an asset of NIS 2.3 million. Against this option there is a forward transaction for the purchase of €10 million at an exercise price of \$1.1766 per euro, with a fair value of an asset of NIS 0.5 million. In addition, a PUT option was sold for the sale of dollars against the euro as follows: €20 million at an exercise price of \$1.25 per euro, with a fair value of a liability of NIS 0.2 million. These transactions are for the period until February 27, 2006.

In addition, Polar Investments has a Call option for the purchase of dollars against the euro as follows: €20 million at an exercise price of \$1.155 per euro, with a fair value of an asset of NIS 0.8 million. A PUT option was sold for the sale of dollars against the euro as follows: €20 million at an exercise price of \$1.205 per euro, with a fair value of a liability of NIS 1.3 million. These transactions were for the period of up to March 22, 2006.

The maximum holding of Polar Investments in derivatives during the period of the report was during the period December 1, 2005 – December 31, 2005 and was a CALL option for the purchase of €40 million against the sale of dollars, a PUT option for the sale of €40 million against the purchase of dollars and a forward transaction for the purchase of €10 million against the sale of dollars.

The maximum holding of a subsidiary of Polar Investments in derivatives during the period of the report was during the period June 23, 2005 – September 30, 2005 and was a PUT option for the sale of €10 million against the purchase of dollars and a forward transaction for the purchase of \$2.5 million. As of the date of this report, the subsidiary of Polar Investments has no holdings in derivatives.

In view of the existence of dollar liabilities on the books of the Company and the private companies under its control, the Company and the private companies under its control from time to time execute hedging transactions on the exposure to changes in the exchange rate of the US dollar. As of December 31, 2005, there were no such hedging transactions opened. The results of these transactions during the period under report were immaterial.

During the reporting period, the Company had forward transactions for the purchase of \$6.5 million against the euro, \$4.0 million against the pound sterling for exercise in October 2005, and \$4.4 million against the shekel for exercise in December 2005. As of the balance sheet date, Leader has no significant positions in derivative financial instruments.

In addition to the above, the Company and Leader operate on their own account and through a subsidiary in the Maof derivatives market by purchasing and selling derivative financial instruments, with the total collateral needed for this activity not to exceed approximately NIS 10 million for each of them. During the reporting period, the amount of collateral to be provided by the Company and Leader was increased to NIS 15 million each. The Company and Leader share the risks, expenses, and revenues from these activities equally.

8. Qualitative report on exposure to market risk and management techniques

A. The individual in the Company who is responsible for managing market risks is the deputy CEO of the Company, Ms. Regina Ungar. The management of risks in companies in which the Company invests is carried out at the level of those companies, mainly by senior officers responsible for financial management.

B. Risk factors, market risks and external factors

- 1.** The Group operates in various areas of the capital market, which are characterized by high volatility, due to, among other things, the influence of governmental political, security and economic factors in Israel and the world, over which the Group has no control. This volatility affects the volume of the public's involvement in the capital market, the volume of security acquisitions in the primary markets, and as a result, the quantity of offerings being offered to the public.
- 2.** There are many institutions that deal in the underwriting area and the management of offerings. During the past years, most of the activity in this area has been concentrated in the hands of a limited number of companies, with fierce competition among them. Since such competition affects the commission rates collected from the issuing companies and the resolution of the values of the issuing companies, it is not inconceivable that, in the future, international investment banks, with organizational and economic resources that exceed those of the Group, will begin operating in this sector.
- 3.** Legislative changes in the area of taxation of securities and changes in laws that relate to revisions in the conventional underwriting process in Israel, could have an effect on the activities of the Group, which cannot be anticipated on the date of issuance of this report.
- 4.** Companies that operate in this sector have civil and criminal exposure in their activities as underwriter, and in particular, when they act as head managers of the underwriting consortium, including exposure to law suits due to misleading details in prospectuses which they have signed. In recent years, legal claims have been filed against different entities in the capital market in relation to their obligations as aforesaid.

5. The Group has made material investments in investee and other companies, part of whose shares are registered for trading on stock exchanges in Israel and/or the world, and accordingly, the market value of the companies is affected, inter alia, by changes and trends in Israeli and world capital markets. The changes in the prices of securities of the public companies that are classified as long-term investments, do not by themselves affect the operating results, shareholders' equity, cash flows or value of the Company. In the case of a decrease in share prices, which are not considered as temporary, the profitability and asset value of the Company could be impaired, directly or indirectly.
6. Part of the companies in the Group rely in their operations on a limited number of significant suppliers and subcontractors, which supply components that are material to their operations. Failure of the suppliers and/or subcontractors to meet the demands of the companies, or termination of arrangements with them, could have a negative effect on these Group companies and endanger their ability to market their products.
7. A portion of the Group companies have investments in companies whose revenues are based to a significant extent on commitments with major customers, major suppliers or specific products, some of which are the result of successful tender offers. Failure to renew these commitments or to win tender offers could have a significant negative effect on the Group's operating results.
8. Part of the Group companies are involved in material law suits or legal proceedings, which if they were to lose, could have a significant effect on the operations of the Group over and above the financial exposure for which provisions have been recorded, and in certain cases, even on their value or likelihood of realization.
9. The Group owns holdings in companies in the advanced technology sector which necessitate significant investments in research and development of goods or services, where it is uncertain whether development will enable it to produce products or services which can be marketed on a commercial basis or whether they will be able to protect the technology and intellectual property that they own. Cumulative failure of these investments by the investees could also have an indirect negative effect on the Group's operating results.

In addition, the Group has made material investments in companies, part of which are in the initial stages of operation, which require large investments and which must cope with severe competitive conditions with well based competitors in the market.

10. The security condition in Israel and the world affects the Group's operating results.
11. The Group is not involved at all in the management of part of the companies in which it has invested, despite that the cumulative amounts invested in them could be material.

12. The Company owns material holdings in companies, the operations of which are conditional upon the provisions of a license or concession from the Ministry of Communications, which could be revoked or not renewed. These licenses and concessions might even place restrictions on the Company regarding changes in ownership, limitations on holdings in competing companies and obligations by the Company to directly and/or indirectly invest in these companies.
13. The Group has residential, commercial and office real estate investments in Israel and abroad which are affected by prices of homes, commercial areas and offices in the real estate markets in Israel and overseas, the availability of sources of financing and territorial policies of the government and other regulatory authorities.
14. Due to the variety of sources of credit of the Group and its affiliates, including those that operate abroad, there is exposure to changes in interest rates, in the rate of inflation and in currency rates that directly influence their liquid assets, liabilities and operating results. Also, an increase in the financial leverage of the Company and affiliates could enlarge these exposures.
15. The Group is exposed to changes in foreign currency rates, since it has assets and liabilities which are not in the reporting currency (balance sheet exposure) and also, since the linkage bases of revenues and expenses do not always correspond (economic exposure).
16. Part of the Group companies are exposed to changes in raw material prices, other prices and other economic indices which have a material effect on the assets or liabilities of these companies, including the companies' liabilities to suppliers, customer debts to the companies, the value of inventories owned, etc.
17. The amounts budgeted by governmental authorities have an effect on the operations of certain Group companies.
18. Certain companies are exposed to numerous requirements of authorities that administer environmental conservation.
19. Some of the Group companies compete in a market along with competitors that have substantial resources for the financing of research and development, marketing, sales and technical support services. In addition, part of the Group companies operate in markets that are characterized by rapid technological changes and frequent introduction of new products by competitors that might change the consumption practices of the customers of these companies. The failure of these companies to meet competition, as described above, could affect their operating results in a negative manner.

C. Description of market risk management policies-

Company Management scrutinizes and takes decisions, under changing conditions and circumstances, with regard to the volume and type of investments, the level of underwriting exposure and the extent and type of leverage of the Company.

The Company, as part of the regulation, supervision and management process of its investment in investee companies, is party to and receives updates of material matters in these companies from Company representatives who act as observers or board and committee members of those companies.

The Company periodically evaluates the composition of its investment portfolio, both from the operational viewpoint and from the standpoint of market value. Additionally, the Company examines the yields of its portfolio of monetary assets from time to time and compares it to

market yields of various avenues while investigating the possibility of changing the composition of the portfolio or of realizing some of its channels.

The Company regards most of the investments in its affiliates as long-term investments, and therefore, does not execute hedging measures against changes in their values or against a decrease in the profitability of these companies.

In order to reduce the exposure to real changes in foreign currency and to changes in NIS interest rates of the Company and its investees, the Company acts to the extent possible to reduce exposure by maintaining a balanced linkage and interest balance sheet for the investee companies.

The risk management policies of the Company, as described above, are carried out principally for the Company itself. The Company does not stipulate or manage the risk policies of its investees. The setting of the risk management policies of the investee companies and the execution thereof are undertaken directly by those companies. Also, the Company does not engage in activities intended to hedge market risks that derive from the operations of its investees and from the investee companies that they hold. Moreover, the Company does not manage the total accumulated market risks and, accordingly, does not offset the market risks of one investee company against those of another investee company.

9. Contributions

The Company regards contributions to the community as an important objective in its business activities and, therefore contributes in equal portions with Leader through the DS Fund, which is a registered association that has been recognized as a not-for-profit organization. The principal purpose of the association, as was set forth upon its establishment is: “to establish a fund in Israel for contributions to charitable institutions and enterprises, to institutions, to the needy and indigent, to educational, cultural, sport, artistic, scientific, research, intellectual institutions and enterprises, for scholarships to students, health, welfare and medicine”. The amount of contributions of the Company and on a consolidated basis (including contributions of the Company’s subsidiaries) during the reporting period was approximately NIS 357 thousand and NIS 1,653 thousand, respectively. The amount of contributions last year, consolidated and Company, was NIS 414 thousand and NIS 1,492 thousand, respectively.

10. Critical accounting policies

The preparation of the financial statements of the Company and its subsidiaries in accordance with accounting principles generally accepted in Israel (GAAP) requires it to make estimates and to assume assumptions that affect the amounts presented in the financial statements. They include estimates that require judgment in an uncertain environment and materially affect the presentation of data in the financial statements.

The following is a description of some of the critical accounting assumptions that are used in preparation of the financial statements which, at the time that they are formulated, require the making of assumptions which in the circumstances and situations, involve significant uncertainties. The Company or subsidiaries, in deciding the determination of the estimates, rely upon past experience, various facts, external factors and reasonable assumptions under circumstances that conform to each estimate. The actual results are likely to differ from these estimates.

- A. The financial statements of Company subsidiaries include deferred tax assets with respect to losses for tax purposes from prior years, the realization of which is expected in the foreseeable future, inter alia, on the basis of anticipated group earnings and on business plans of certain subsidiaries, according to which the realization of the tax benefits from the tax losses in these companies is expected. It is acknowledged that the actual fulfillment of these forecasts could vary and that, accordingly, the matter could affect the realization of the tax benefits in the future.
- B. In accordance with the provisions of Accounting Standard No. 15 of the Israeli Accounting Standards Board, the Company and its subsidiaries, as the case may be, as of each balance sheet

date, analyze whether events have occurred or changes in circumstances have taken place which indicate that there has been a decline in value of one or more of the non-monetary assets to which the Standard applies. If indications of a decline in value should exist, the Company and the subsidiaries consider whether, in such case, the amount at which the investment in the asset is presented is recoverable out of the anticipated cash flows from that asset, and to the extent necessary, record a provision for decline in value to the extent of the unrecoverable amount of the asset.

Determination of the estimates of the cash flows is based on past experience with this asset or similar assets, and on the best judgment of the Company and subsidiaries, as the case may be, of the economic conditions that will be present during the balance of the useful life of the asset. In determining the net sales price of part of the assets, the Company uses valuations performed by appraisers for real estate assets. The estimates also take into account the condition of the market in the vicinity in which the asset is located.

Intensification of competition in the markets in which the Company and the subsidiaries operate might materially affect the cash flow forecasts, the balance of the useful life and the determination of the net sales price of the asset.

11. Auditing fees

The fees paid by the Company and the private companies under its control to Somekh Haikin & Co., CPAs (Isr.), in respect of auditing services, services related to the audit, and ongoing tax work in 2005, amounted to NIS 430 thousand, compared with NIS 460 thousand in 2004. In respect of additional services, including special tax work, the fees amounted to NIS 200 thousand (including in respect of a prospectus), compared with NIS 378 thousand in 2004 (mostly to Kost Firer Gabbai and Kasirer).

We present below a breakdown of the auditing fees of the material subsidiaries of the Company, in respect of auditing services, audit-related services and tax work in 2005:

	NIS'000 (*)	Auditor
Leader and its privately controlled companies	520	Kost Firer Gabbai and Kasirer
Technologies	253	Somekh Haikin
Danbar Technologies	74	Brightman Almagor
Platinum Fund	77	Kost Firer Gabbai and Kasirer
DS Polaris	43	Somekh Haikin
Urdan	610	Brightman Almagor
Itong	380	Brightman Almagor
Univerkal	335	Brightman Almagor
Aloni	135	Brightman Almagor
Polar Investments	375	Somekh Haikin
Polar Communications	154	Brightman Almagor
Polar Real Estate	248	Zohar and Zohar
Polar International Real Estate	150	Zohar and Zohar
Telit	644	Baker Tilly
Dai Telecom	839	Deloitte
Ofir Holdings	146	Kesselman & Kesselman
Hazera	89	Kesselman & Kesselman
Nipson	490	Baker Tilly

(*) In addition, an amount of NIS 812 thousand was paid by these companies for additional services.

12. Peer review

On July 28, 2005, the Israel Securities Authority issued a guideline in accordance with article 36A of the Israeli Securities Law – 1968 in the matter of disclosure pertaining to the agreement to conduct a peer review, the goal of which, according to the guideline, is to initiate a control process regarding the work of accounting firms, and an assessment of the existence of procedures required during the course of the work carried out by such firms, which would contribute to the existence of an advanced capital market.

The board of directors of the Company granted its consent to have the peer review carried out.

13. Disclosure regarding the internal auditor of the entity

A. Identity of the internal auditor

Ezra Yehuda, CPA, is the Company's internal auditor and was appointed to this position on July 29, 1993. The internal auditor is the owner of an auditing firm that specializes in internal auditing. The firm has 17 years of experience in performing internal auditing in public companies and it specialized in a wide variety of areas of activity. The internal auditor is not an employee of the Company, but provides it with external internal auditing services.

B. Scope of service of the internal auditor

The scope of the work of the internal auditor and his staff is approximately 150 hours per year, on the average.

C. Audit plan

The annual and multi-year audit plan is presented by the internal auditor to the Company's Audit Committee. The Audit Committee scrutinizes the issues in consultation with management of the Company, and subsequently decides on the approval of the audit plan (with or without changes). The considerations that guide the Audit Committee are, among other things, the needs of the audit, the importance of the issues, the frequency in which the issues were examined in previous years and the recommendations of the internal auditor.

D. The professional standards guiding the performance of the audit

In accordance with the notification of the Company's internal auditor, he performed his audit in accordance with accepted professional standards under Section 4(b) of the Internal Audit Law, 1992.

E. The identity of the person responsible for the internal auditor

The Chairman of the Board is responsible for the internal auditor on the Company's behalf.

F. Meetings of the Audit Committee during 2005

During 2005, one audit report was prepared by the internal auditor. The discussion of the report's findings in the Company's Audit Committee took place on May 22, 2005 and an additional meeting of the Audit Committee was held on August 16, 2005.

G. The extent and substance of the work program of the internal auditor are reasonable under the circumstances and are adequate to carry out the purposes of the internal audit, because the issues selected are material to the Company and were examined from different aspects. The internal auditor was given continual and unlimited autonomy with regard to all of the Company's information systems, including access to financial data of the Company, under Section 9 of the Internal Audit Law, 1992.

14. Report of linkage bases (in millions of reported:

As of December 31, 2005	Financial balances			Non-financial balances	Total
	Unlinked	Linked to the CPI	In or linked to foreign currency(*)		
Assets:					
Cash and cash equivalents	351.6	-	225.2	-	576.8
Marketable securities	369.2	4.5	76.0	-	449.7
Short-term deposits and investments	-	2.0	33.5	-	35.5
Current maturities and loans granted	-	14.9	-	-	14.9
Trade accounts receivable	122.8	1.0	172.9	258.7	555.4
Accounts receivable and other debit balances	59.3	26.2	44.8	12.8	143.1
Inventory and work in progress	-	-	-	366.3	366.3
Real estate	-	-	-	634.1	634.1
Long-term investments in investee and other companies	39.4	130.8	77.7	374.3	622.2
Long-term deposits and loans granted	6.4	107.1	0.9	-	114.4
Fixed assets, net	-	-	-	646.6	646.6
Other assets and deferred expenses	-	-	-	135.4	135.4
Total assets	948.7	286.5	631.0	2,428.2	4,294.4
Liabilities:					
Short-term credit from banks and others	412.8	329.5	127.5	-	869.8
Suppliers	121.3	9.0	110.0	0.7	241.0
Accounts payable	172.0	44.9	52.8	10.1	279.8
Advances from customers	98.2	-	-	-	98.2
Long-term liabilities to banks and others	366.2	483.5	198.3	-	1,048.0
Debentures	-	510.5	61.5	-	572.0
Convertible debentures	-	138.1	11.6	-	149.7
Severance pay	0.8	-	-	12.2	13.0
Deferred taxes	-	-	-	10.8	10.8
Long-term liabilities	1,171.3	1,515.5	561.7	33.8	3,282.3
Minority interests	-	-	-	717.8	717.8
Receipts in respect of options issued in subsidiaries	1.8	-	-	14.2	16.0
Debentures convertible into shares (quasi-equity)	-	-	-	11.7	11.7
Shareholders' equity	-	-	-	266.6	266.6
	1.8	-	-	1,010.3	1,012.1
	1,173.1	1,515.5	561.7	1,044.1	4,294.4
	(224.4)	(1,229.0)	69.3	1,384.1	-

(*) Mainly US dollar.

Report of linkage bases (in millions of reported and adjusted NIS for the years 2005 and 2004, respectively):

As of December 31, 2004	Financial balances				Total
	Unlinked	Linked to the CPI	In or linked to foreign currency(**)	Non-financial balances	
Assets:					
Cash and cash equivalents	103.3	2.5	105.6	-	211.4
Marketable securities	182.7	9.0	68.0	-	259.7
Short-term deposits and investments	9.1	0.2	-	-	9.3
Current maturities and loans granted	19.7	14.9	6.5	-	41.1
Trade accounts receivable	402.8	-	147.3	-	550.1
Accounts receivable and other debit balances	(*)82.2	11.0	33.6	35.2	(*)162.0
Inventory and work in progress	-	-	-	351.8	351.8
Real estate	-	-	-	452.2	452.2
Long-term investments in investee and other companies	50.2	153.6	53.3	494.1	751.2
Long-term deposits and loans granted	3.5	19.1	76.2	-	98.8
Fixed assets, net	0.2	-	-	710.9	711.1
Other assets and deferred expenses	-	-	-	140.1	140.1
Total assets	853.7	210.3	490.5	2,184.3	3,738.8
Liabilities:					
Short-term credit from banks and others	683.2	299.9	78.4	-	1,061.5
Suppliers	114.0	8.6	92.9	0.6	216.1
Accounts payable	(*)151.8	25.9	60.4	26.2	(*)264.3
Advances from customers	61.8	-	-	-	61.8
Long-term liabilities to banks and others	475.0	531.2	82.0	-	1,088.2
Debentures	42.9	90.8	-	-	133.7
Convertible debentures	-	130.6	30.1	-	160.7
Receipts in respect of options issued in subsidiaries	2.6	-	-	15.0	17.6
Deferred taxes	-	-	-	22.4	22.4
Long-term liabilities	1,531.3	1,087.0	343.8	64.2	3,026.3
Minority interests	-	-	-	(*)477.7	(*)477.7
Receipts in respect of options issued in subsidiaries	-	-	-	11.0	11.0
Shareholders' equity	-	-	-	(*)223.8	(*)223.8
	1,531.3	1,087.0	343.8	712.5	712.5
	1,531.3	1,087.0	343.8	776.7	3,738.8
	(677.6)	(876.7)	146.7	1,407.6	-

(*) The financial statements were restated – see Note 2AA of the financial statements.

(**) Mainly US dollar.

The Company thanks its employees for their involvement with the Company and its shareholders for their trust.

Itschak Shrem-Chairman of the Board

Yair Fudim, CEO and Director

Date: March 27, 2006

Shrem, Fudim, Kelner & Co. Ltd.

**Financial Statements
As at December 31, 2005**

Balance Sheets as at December 31**Reported amounts****

	Consolidated		Company	
	2005	2004	2005	2004
	NIS thousands	NIS thousands	NIS thousands	NIS thousands
Current assets				
Cash and cash equivalents	576,785	211,371	54,688	9,857
Deposits and short-term investments	35,447	9,337	-	-
Marketable securities	449,732	259,737	64,345	59,800
Current maturities and loans receivable	14,896	41,133	89	172
Trade receivables	555,417	550,086	242	310
Other receivables	143,109	*162,007	14,014	16,069
Inventory and work in process	366,287	351,795	-	-
	2,141,673	1,585,466	133,378	86,208
Real estate	634,111	452,186	-	-
Investments and long-term loans				
Investments in investee and other companies	622,154	751,222	331,056	*305,539
Deposits and loans	114,415	98,770	391	721
	736,569	849,992	331,447	306,260
Fixed assets	646,574	711,056	23,728	24,666
Other assets and deferred expenses	135,401	140,078	2,148	-
	4,294,328	3,738,778	490,701	417,134

* Restated

** In respect of discontinuance of adjustment for the effect of inflation according to the CPI of December 31, 2003.

Date of approval: March 27, 2006

Balance Sheets as at December 31**Reported amounts****

	Consolidated		Company	
	2005	2004	2005	2004
	NIS thousands	NIS thousands	NIS thousands	NIS thousands
Current liabilities				
Credit from banks and others	869,677	1,061,530	50,939	101,986
Suppliers and service providers	241,005	216,105	476	613
Accounts payable and credit balances	279,799	** 264,286	26,317	* 23,074
Customer deposits	98,212	61,758	-	-
	1,488,693	1,603,679	77,732	125,673
Long-term liabilities				
Credit from banks and others	1,048,030	1,088,223	33,401	* 55,002
Debentures	571,945	133,652	89,141	-
Convertible debentures	149,692	160,661	11,598	12,348
Employee retirement benefit, net	13,030	17,591	460	317
Deferred tax	10,821	22,400	-	-
	1,793,518	1,422,527	134,600	67,667
Minority interest	717,802	** 477,735	-	-
Convertible debentures	11,727	-	11,727	-
Receipts from share options issued by subsidiaries	15,946	11,043	-	-
Shareholders' equity	266,642	** 223,794	266,642	** 223,794
	4,294,328	3,738,778	490,701	417,134

* Reclassified

** Restated

*** In respect of discontinuance of adjustment for the effect of inflation according to the CPI of December 31, 2003.

Statements of Operations for the Year Ended December 31

	Consolidated			Company		
	For the year ended December 31			For the year ended December 31		
	2005	2004	2003	2005	2004	2002
		Amounts adjusted to the effect of inflation in terms of December 31 2003			Amounts adjusted to the effect of inflation in terms of December 31 2003	
	Reported Amounts **	Reported Amounts **	Reported Amounts **	Reported Amounts **	Reported Amounts **	Reported Amounts **
	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands
Income						
Sales, management, consultancy services and Underwriting	1,903,522	*1,814,020	*1,368,323	7,979	9,216	17,789
Gain on marketable securities, net	66,779	44,623	110,536	16,006	14,870	17,566
Gain on sale of investments, loans and assets, net	357,164	158,962	-	8,600	2,369	4,899
Company's equity in earnings of investees, net	-	37,659	10,857	61,725	* 54,188	-
	2,327,465	2,055,264	1,489,716	94,310	80,643	40,254
Costs and expenses						
Cost of sales and services	1,464,786	1,365,868	999,130	1,428	2,224	959
Selling and marketing	202,650	173,808	159,371	-	-	-
Administrative and general	268,800	* 251,550	* 228,059	23,475	18,669	28,645
Loss on sale of investment loans and assets, net	-	-	1,402	-	-	-
Company's equity in losses of investees, net	21,942	-	-	-	-	32,277
Financing expenses, net	160,983	140,934	177,620	11,094	11,348	10,690
	2,119,161	1,932,160	1,565,582	35,997	32,241	72,571
Profit (loss) from operations before taxes on income	208,304	123,104	(75,866)	58,313	48,402	(32,317)
Taxes on income	67,987	* 16,494	16,287	(214)	-	580
Profit (loss) from operations after taxes on income	140,317	106,610	(92,153)	58,527	48,402	(32,897)
Minority interest in (earnings) losses of subsidiaries, net	(81,790)	*(58,208)	68,985	-	-	-
Gain (loss) attributed to continued operations	58,527	48,802	(23,168)	58,527	48,402	(32,897)
Gain (loss) attributed to discontinued operations	-	-	(9,729)	-	-	-
Net profit (loss) for the year	58,527	48,802	(32,897)	58,527	48,402	(32,897)

* Restated

** In respect of discontinuance of adjustment for the effect of inflation according to the CPI of December 31, 2003.

Statements of Operations for the Year Ended December 31 (cont'd)

	<u>NIS</u>	<u>NIS</u>	<u>NIS</u>	<u>NIS</u>	<u>NIS</u>	<u>NIS</u>
Earnings (loss) per NIS 1 par value of the share capital:						
Primary gain (loss) per share attributed to continued operations	3.02	*2.64	(1.40)	3.02	*2.64	(1.98)
Primary gain (loss) per share attributed to discontinued operations	-	-	(0.58)	-	-	-
Primary gain (loss) per share	<u>3.02</u>	<u>2.64</u>	<u>(1.98)</u>	<u>3.02</u>	<u>2.64</u>	<u>(1.98)</u>
Fully-diluted gain (loss) per share attributed to continued operations	2.76	*2.37	(1.40)	2.76	*2.37	(1.98)
Fully-diluted gain (loss) per share attributed to discontinued operations	-	-	(0.58)	-	-	-
Primary gain (loss) per share	<u>2.76</u>	<u>2.37</u>	<u>(1.98)</u>	<u>2.76</u>	<u>2.37</u>	<u>(1.98)</u>

* Restated

Statement of Shareholders' Equity

	Share capital	Premium on shares and capital reserves	Receipts from issuance of options	Adjustments from the translation of financial statements of autonomous foreign investees	Loans to employees for purchase of shares	Company shares held by the Company and subsidiary	Dividend declared subsequent to balance sheet date	Retained earnings	Total
	Reported amounts*								
	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands
Balance as at January 1, 2005	25,360	164,850	-	8,670	(3,194)	(2,451)	-	**30,559	**223,794
Changes in 2005:									
Issuance of options	-	-	3,201	-	-	-	-	-	3,201
Purchase of company shares	-	-	-	-	-	(4,849)	-	-	(4,849)
Capital reserves of investee company	-	486	-	-	-	-	-	-	486
Repayment of loan to employees for purchase of shares	-	-	-	-	1,995	-	-	-	1,995
Dividend	-	-	-	-	-	-	-	(9,131)	(9,131)
Conversion of debentures into shares of the Company	188	1,203	-	-	-	-	-	-	1,391
Adjustments from the translation of financial statements of autonomous foreign investees	-	-	-	(8,772)	-	-	-	-	(8,772)
Dividend declared subsequent to balance sheet date	-	-	-	-	-	-	15,000	(15,000)	-
Net profit for the year	-	-	-	-	-	-	-	58,527	58,527
Balance as at December 31, 2005	25,548	166,539	3,201	(102)	(1,199)	(7,300)	15,000	64,955	266,642

* In respect of discontinuance of adjustment for the effect of inflation according to the CPI of December 31, 2003.

** Restated

Statement of Shareholders' Equity (cont'd)

	Share capital	Premium on shares and capital reserves	Adjustments from the translation of financial statements of autonomous foreign investees	Loans to employees for purchase of shares	Company shares held by the Company and subsidiary	Retained earnings	Total
	Reported amounts (*)						
	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands
Balance as at January 1, 2004	24,923	162,223	4,981	(3,194)	(4,691)	(17,464)	166,778
Changes in 2004:							
Sale of Company shares	-	-	-	-	2,240	(379)	1,861
Conversion of debentures into shares of the Company	437	2,876	-	-	-	-	3,313
Changes in capital reserves in respect of investee companies	-	(249)	-	-	-	-	(249)
Adjustments from the translation of financial statements of autonomous foreign investees	-	-	3,689	-	-	-	3,689
Net profit for the year	-	-	-	-	-	(**)48,402	(**)48,402
Balance as at December 31, 2004	25,360	164,850	8,670	(3,194)	(2,451)	30,559	223,794

* In respect of discontinuance of adjustment for the effect of inflation according to the CPI of December 31, 2003.

** Restated

Statement of Shareholders' Equity (cont'd)

	Share capital	Premium on shares and capital reserves	Adjustments from the translation of financial statements of autonomous foreign investees	Loans to employees for purchase of shares	Company shares held by the Company and subsidiary	Retained earnings	Total
Amounts adjusted to the effect of inflation in terms of NIS of December 2003							
	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands
Balance as at January 1, 2003	21,917	137,332	3,354	(3,194)	(4,585)	15,433	170,257
Changes in 2003:							
Private issuance of shares, net	3,006	26,118	-	-	-	-	29,124
Purchase of Company shares by subsidiary	-	-	-	-	(106)	-	(106)
Changes in capital reserves in respect of investee companies	-	(1,227)	-	-	-	-	(1,227)
Adjustments from the translation of financial statements of autonomous foreign investees	-	-	1,627	-	-	-	1,627
Loss for the year	-	-	-	-	-	(32,897)	(32,897)
Balance as at December 31, 2003	<u>24,923</u>	<u>162,223</u>	<u>4,981</u>	<u>(3,194)</u>	<u>(4,691)</u>	<u>(17,464)</u>	<u>166,778</u>

Statements of Cash Flows for the Year Ended December 31

	Consolidated			Company		
	For the year ended December 31			For the year ended December 31		
	2005	2004	2003	2005	2004	2002
		Amounts adjusted to the effect of inflation in terms of December 31 2003			Amounts adjusted to the effect of inflation in terms of December 31 2003	
	Reported Amounts **	Reported Amounts **	Reported Amounts **	Reported Amounts **	Reported Amounts **	Reported Amounts **
	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands
Cash flows from operating activities:						
Net profit (loss) for the year	58,527	* 48,402	(32,897)	58,527	* 48,402	(32,897)
Adjustments required to reconcile cash from operating activities (Annex A)	(102,332)	*(288,088)	(54,880)	(88,451)	*(68,703)	40,090
Net cash inflow (outflow) attributed to continued operations	(43,805)	(239,686)	(87,777)	(29,924)	(20,301)	7,193
Net cash inflow (outflow) attributed to discontinued operations	-	-	14,983	-	-	-
Net cash inflow (outflow) from operating activities	(43,805)	(239,686)	(72,794)	(29,924)	(20,301)	7,193
Cash flows from investing activities:						
Acquisition of fixed assets, real estate and amounts charged to projects under construction and other assets	(231,428)	(83,608)	(108,278)	(623)	(564)	(479)
Proceeds from sale of fixed assets and other assets	111,309	178,266	24,735	238	195	303
Proceeds (purchase) of marketable securities, short-term investment and deposits, net	(150,711)	91,560	90,655	11,874	23,266	(24,781)
Investment in investee and other companies (including through loans and capital notes, net)	(128,333)	(144,644)	(145,104)	(9,818)	(34,080)	(21,803)
Repayment (granting) of loans and deposit, net	(38,622)	(42,021)	22,058	-	30,273	(104)
Proceeds from sale of investments in investee and other companies	467,535	367,532	218,275	49,881	26,797	21,738
Dividend from subsidiary and others	-	-	795	-	-	-
Initially fully or proportionately consolidated companies and acquisition of activities (Annex C)	7	(1,445)	33,724	-	-	-
Companies formerly fully or proportionately consolidated no longer consolidated and activities sold (Annex D)	6,689	665	29,689	-	-	-
Company initially consolidated (Annex E)	(2,690)	-	-	-	-	-
Net cash inflow (outflow) attributed to continued investment activities	33,756	366,305	166,549	51,552	45,887	(25,126)
Net cash inflow (outflow) attributed to discontinued investment activities	-	-	108,371	-	-	-
Net cash inflow (outflow) from investment activities	33,756	366,305	274,920	51,552	45,887	(25,126)

* Restated

** In respect of discontinuance of adjustment for the effect of inflation according to the CPI of December 31, 2003.

Statements of Cash Flows for the Year Ended December 31 (cont'd)

	Consolidated			Company		
	For the year ended December 31			For the year ended December 31		
	2005	2004	2003	2005	2004	2002
			Amounts adjusted to the effect of inflation in terms of			Amounts adjusted to the effect of inflation in terms of
	Reported Amounts **	Reported Amounts **	December 31 2003	Reported Amounts **	Reported Amounts **	December 31 2003
	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands
Cash flows from financing activities:						
Repayment of loans for the purchase of company shares	1,995			1,995		
Issuance of shares and option warrants	3,201	-	-	3,201	-	-
Sell of Company's shares	-	1,861	-	-	-	-
Purchase of Treasury shares	(4,849)	-	(106)	-	234	-
Purchase of minority shares	-	-	-	-	-	-
Repayment of long-term loan received from the sellers of a subsidiary		-	-		-	-
Issue of convertible bonds in Company's shares, net	67,912	-	11,640	94,912	-	11,640
Long-term loans and capital notes, net	(238,869)	(109,918)	45,307	(16,362)	(18,675)	48,098
Issue of debentures and convertible debentures in consolidated companies, net	63,479	-	35,884	-	-	-
Repayment of debentures and convertible debentures in consolidated companies	(131,989)	(85,342)	(96,228)	-	-	-
Dividend to minority	(35,277)	(23,603)	(1,341)	-	-	-
Issue of marketable securities of subsidiaries	725,081	55,073	(1,262)	-	-	-
Liability for financial lease	-	(53,850)	(54,739)	-	-	-
Dividend	(9,131)	-	-	(9,131)	-	-
Receipt (repayment) of short-term credit, net	(52,963)	11,592	(10,007)	(51,412)	1,980	(43,221)
Net cash inflow (outflow) attributed to continued financing activities	388,590	(204,187)	(70,852)	23,203	(16,461)	16,517
Net cash inflow (outflow) attributed to discontinued financing activities	-	-	(117,385)	-	-	-
Net cash inflow (outflow) from financing activities	388,590	(204,187)	(188,237)	23,203	(16,461)	16,517
Translation differences with respect to cash balances in autonomous investee companies	(13,127)	(579)	(999)	-	-	-
Increase (decrease) in cash and cash equivalents	365,414	(78,147)	6,921	44,831	9,125	(1,416)
Balance of cash and cash equivalents at beginning of year	211,371	289,518	282,597	9,857	732	2,148
Balance of cash and cash equivalents as at end of year	576,785	211,371	289,518	54,688	9,857	732

** In respect of discontinuance of adjustment for the effect of inflation according to the CPI of December 31, 2003.

Statements of Cash Flows for the Year Ended December 31 (cont'd)

	Consolidated			Company		
	For the year ended December 31			For the year ended December 31		
	2005	2004	2003	2005	2004	2002
			Amounts adjusted to the effect of inflation in terms of December 31 2003			Amounts adjusted to the effect of inflation in terms of December 31 2003
	Reported Amounts **	Reported Amounts **		Reported Amounts **	Reported Amounts **	
	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands
Annex A -						
Adjustments required to reconcile cash from operating activities						
Income and expenses not involving cash flows:						
Loss attributed to discontinued operations	-	-	9,729	-	-	-
Depreciation and amortization	78,033	55,293	69,007	1,940	1,396	1,390
Company's equity in losses (earnings) of investee companies less of dividend received, net	27,182	(19,897)	6,815	(28,932)	(45,966)	36,069
Deferred taxes, net	42,011	2,769	(10,480)	-	-	147
Minority interest in earnings (losses) of subsidiaries, net	81,790	* 58,208	(68,985)	-	-	-
Loss (gain) on marketable securities, net	(56,703)	(18,669)	(91,597)	(16,006)	(14,870)	(17,566)
Increase (decrease) in liability for employee severance benefits, net	(3,450)	25	(3,259)	143	1	(127)
Loss (gain) on sale and amortization of long-term investments and assets, net	(366,166)	(162,584)	(17,022)	(7,379)	(3,140)	(3,088)
Expenses (income) from financing activities	27,405	8,088	8,874	(1,446)	28	690
Other expenses		6,782	17,839		-	-
Changes in asset and liability items:						
Decrease (increase) in trade receivables and other receivables	(23,393)	*(143,443)	(602)	(39,877)	(8,678)	2,408
Decrease (increase) in inventory and work in process, net	(23,869)	(21,927)	16,466	-	-	-
Increase (decrease) in suppliers and service providers	114,828	*(52,733)	8,335	3,106	2,526	20,167
	(102,332)	(288,088)	(54,880)	(88,451)	(68,703)	40,090

* Restated

** In respect of discontinuance of adjustment for the effect of inflation according to the CPI of December 31, 2003.

Statements of Cash Flows for the Year Ended December 31 (cont'd)**Annex B - Non cash transactions**

	Consolidated			Company		
	For the year ended December 31			For the year ended December 31		
	2005	2004	2003	2005	2004	2002
	Reported Amounts **	Reported Amounts **	Amounts adjusted to the effect of inflation in terms of December 31 2003	Reported Amounts **	Reported Amounts **	Amounts adjusted to the effect of inflation in terms of December 31 2003
NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	
Purchase of Treasury stocks and option warrants in exchange of redemption loans to employees	-	-	25,552	-	-	-
Commitment to invest in other companies	84	527	1,397	-	-	-
Investments in a subsidiary in respect of issuance of shares	-	-	36,575	-	-	36,575
Purchase of fixed assets on credit	1,468	2,481	4,221	-	-	-
Purchase of the minority interest in a subsidiary against the issuance of shares, options and debentures of another subsidiary	-	-	24,687	-	-	-
Amounts receivable	-	-	75,158	-	-	-
Conversion of debentures into shares of Company	1,391	3,313	-	1,391	3,313	-
Conversion of debentures into shares of subsidiary	32,532	-	-	-	-	-
Sale of fixed assets on credit	10,438	-	-	-	-	-
Proceeds from sale of investment in investee	-	1,290	1,571	-	703	-

** In respect of discontinuance of adjustment for the effect of inflation according to the CPI of December 31, 2003.

Statements of Cash Flows for the Year Ended December 31 (cont'd)**Annex C - Initially fully or proportionately consolidated companies and acquisition of activities**

	Consolidated		
	2005	2004	2003
	Reported Amounts * NIS thousands	Reported Amounts * NIS thousands	Amounts adjusted to the effect of inflation in terms of NIS of December 2003 NIS thousands
Working capital, net (excluding cash and cash equivalents)	1,279	2,105	38,084
Investments, long-term loans and fixed assets	-	(3,550)	(19,194)
Other assets and deferred expenses	-	-	(17,816)
Long-term liabilities	2,421	-	68,533
Excess cost	(10,502)	-	(37,463)
Balance of investment in companies as at date of initial consolidated	8,235	-	1,580
Minority share in deficiency	(1,426)	-	-
	7	(1,445)	33,724

Annex D - Companies previously consolidated, fully or proportionately, which are no longer consolidated and activity sold

	Consolidated		
	2005	2004	2003
	Reported Amounts * NIS thousands	Reported Amounts * NIS thousands	Amounts adjusted to the effect of inflation in terms of NIS of December 2003 NIS thousands
Working capital, net (excluding cash and cash equivalents)	(30,672)	(664)	42,204
Investments and long-term loans	16,467	-	1,366
Fixed and other assets	17,672	1,228	14,944
Long-term liabilities	(1,254)	(100)	(6,101)
Minority interest	(7,971)	220	(25,050)
Balance of loans and investments which left at the time of exit from consolidation	(18,080)	1,427	(10,622)
Capital gain (loss) on sale or issuance to third party	33,059	(1,446)	12,948
Proceeds on credit	(2,532)	-	-
	6,689	665	29,689

* In respect of discontinuance of adjustment for the effect of inflation according to the CPI of December 31, 2003.

Statements of Cash Flows for the Year Ended December 31 (cont'd)**Annex E - Company initially consolidated**

	Consolidated		
	2005	2004	2003
	Reported Amounts *	Reported Amounts *	Amounts adjusted to the effect of inflation in terms of NIS of December 2003
	NIS thousands	NIS thousands	NIS thousands
Working capital, net (excluding cash and cash equivalents)	10,093	-	-
Fixed assets, net	(7,908)	-	-
Goodwill created upon acquisition	(2,209)	-	-
Long-term investments and debits	211	-	-
Other assets, net	(3,883)	-	-
Long term liabilities	1,006	-	-
	(2,690)	-	-

** In respect of discontinuance of adjustment for the effect of inflation according to the CPI of December 31, 2003.