

AFRICA ISRAEL PROPERTIES LTD.

CORPORATION'S BUSINESS DESCRIPTION

CORPORATION BUSINESS DESCRIPTION - TABLE OF CONTENTS

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This report includes prospective information, as defined in the Securities Law, 1968. Such information contain, inter alia, forecasts, objectives and company's valuations and estimates that relate to future events or conditions, whose materialization is uncertain and beyond the company's control. Prospective information presented in this report will be usually identified by phrases such as "the company anticipates", "the company expects", "the company estimates", "the company believes", "the company intends", and by similar expressions.

Prospective information is not a demonstrated fact; it is based only on the point of view held by the company's management springing from an analysis of the general information possessed by the company's management at the date of this report. Prospective information is, by its very nature, liable to the risk of significant non-materialization and such information is, as explained, uncertain, not given to prior evaluation, and sometimes is even beyond the company's control.

The prospective information presented in this report may rely on public publications, studies and surveys, claimed by their writers to be based on sources considered reliable, but the information contained in them is not vouched for by their writers or editors to be correct and/or complete. While the company believes that these publications are reliable, the correctness of the information contained in them has never been independently examined by the company's management.

In addition, materialization of the prospective information will be influenced by the risk factors which characterized the company's activities, as presented in detail further below in the this report, as well as by developments of the general environment and in external factors affecting the company's activities, that cannot be estimated beforehand and by their very nature are outside the field controlled by the company.

For these reasons, although the company management believed that its expectations, as presented in this prospective information, are reasonable indeed, the readers of this report, including investors and shareholders, are hereby warned that the future actual results and attainments of the company might be materially different from those provided in the prospective information presented in this report.

The prospective information presented in this report pertains only to the date of its writing, and the company does not undertake to update or change it as it receives further information relating to the above information.

CHAPTER 1 – THE GENERAL DEVELOPMENT OF THE CORPORATION'S BUSINESS DESCRIBED

1. THE CORPORATION'S ACTIVITIES AND DESCRIPTION OF THE DEVELOPMENT OF ITS BUSINESS

- 1.1 Africa Israel Properties Ltd. (above and hereinafter: "**the company**" or "**the corporation**") was incorporated in 1971 as a private company. The company went public in September 2004 and its securities were listed for trade on the Tel Aviv Stock Exchange for the first time.

The company is a subsidiary of Africa Israel Investments Ltd. (hereinafter - "**Africa Investments**"). Africa Investments is a public company whose shares are listed for trade on the TASE. It is controlled by Mr. Lev Leviev. On February 14, 2006, Africa Investments gave notice, in an immediate report, that Mr. Lev Leviev and/or companies wholly owned and controlled by him, (hereinafter - "**the purchaser**"), had signed an agreement with Bank Leumi Israel Ltd., a public company whose shares are listed for trade on the TASE, (hereinafter - "**Bank Leumi**"), regarding the acquisition of the holdings of Bank Leumi in Africa Investments. Upon completion of the aforementioned transaction, Bank Leumi would cease to be an interested party in Africa Investments and the holdings of Mr. Lev Leviev in Africa Investments (indirectly by virtue of companies under his control), are expected to amount to approximately 79.95% in capital and voting rights (about 76.26% on a fully-diluted basis).

As at the date of this report Bank Leumi holds (by means of a wholly owned subsidiary) approximately 5% of the issued share capital and voting rights in the company (approximately 4% on a fully diluted basis).

- 1.2 The company acts, by itself and through its investee companies (the company and the investee companies are called hereinafter: "**the company group**" or "**the group**"), to initiate, construct, rent and operate industrial, office, and commercial buildings, in Israel and abroad.

Until 2002, the company's principal activity consisted in initiating and constructing rental real estate properties in Israel, especially industrial and office buildings.

During the years 2002 and 2003, Africa Investments and companies under its control (hereinafter - "**Africa Investments group**") carried out a reorganization of the holdings in corporations it holds, corporations which hold real estate properties in Israel and abroad, for the purpose of concentrating within the company's framework the major part of the income-generating real estate activities in Israel and part of the income-generating real estate activities abroad.

Within the framework of this reorganization, part of Africa Investments activities abroad, previously carried out by corporations directly or indirectly held by Africa Investments and not through the company, was transferred to the company. Also within the framework of this organization, Africa Israel International Properties (2002) Ltd. (hereinafter -

"**International Properties**"), a company registered in Israel and wholly owned and controlled by the company, was founded. Africa Investments group holdings in Africa Investments held foreign corporations, of properties abroad, were transferred to this new company. The activities of Africa Investments in the USA were not transferred to a member-company of the Africa Investments group for various reasons, one of them being the fact that activities in the USA were of a mixed orientation – for sale as well as for rent – and Africa Investments had decided to keep them separated. Likewise, no Africa Investments group activities in Russia were transferred to any of the group companies, because of the unique characteristics of activities in this region and Africa Investments' decision to keep them separated as well.

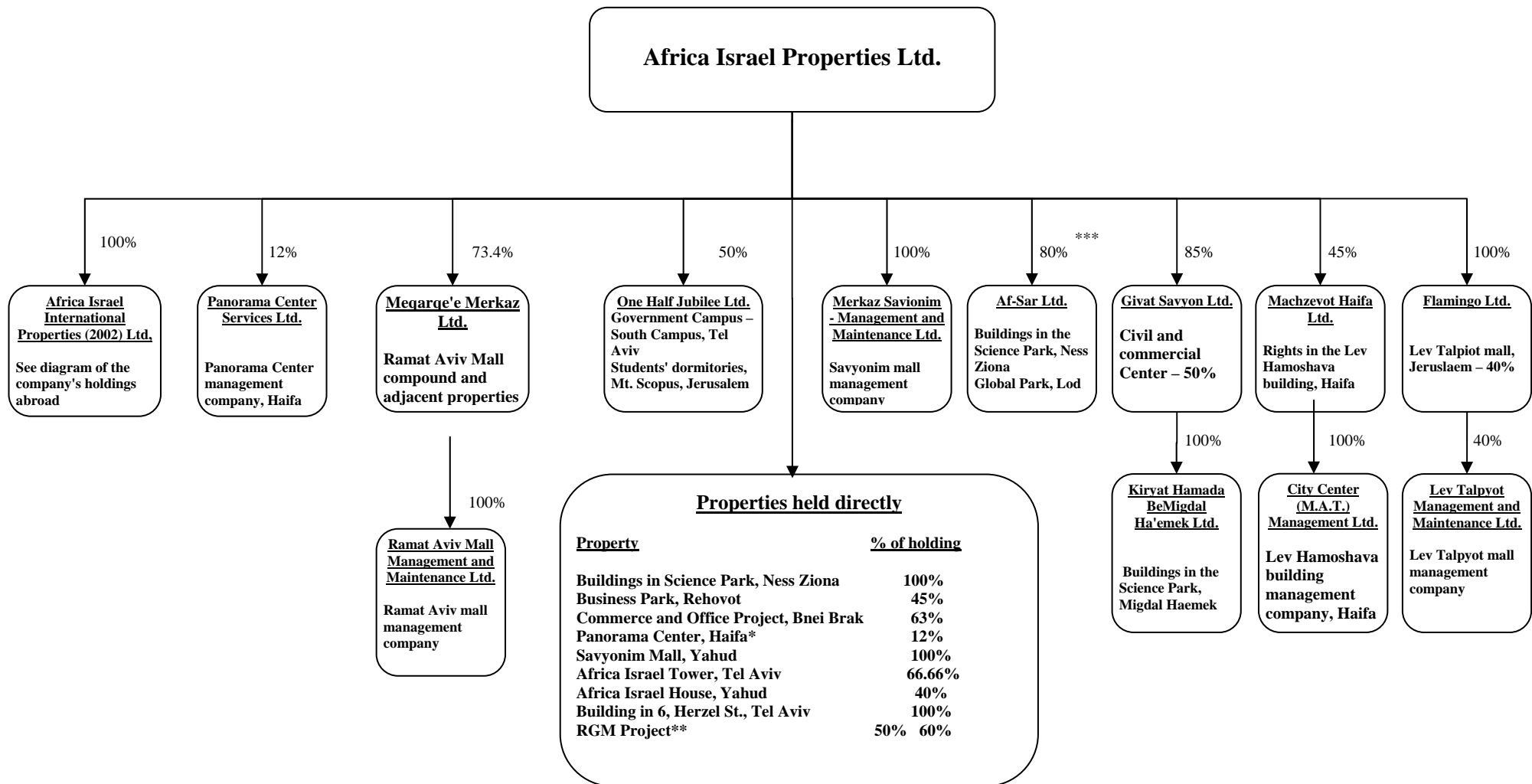
An agreement between the company and Africa Investments was signed on December 31, 2003. Its purpose was to concentrate within the company's framework the major part of income-generating real estate activity in Israel, by transfer to the company of real estate properties and shares of Africa Investments held corporations. The transferred properties are mostly income-generating real estate properties, held directly by Africa Investments or by Africa Investments held companies.

The company first published a securities issue prospectus in September 2004, of its securities that were listed for trade in the TASE.

Today, the company is active both in Israel and abroad. The company group owns office, industrial and commercial-space buildings in Israel and abroad. As at the date of the report, the company carries on its activities in Israel, the Czech Republic, Holland, Canada, Serbia and Romania. The company sold its operation in Canada after the date of the balance sheet and commenced operations in the Philippines

- 1.3 Following is a diagram of the structure of the company's holdings in active companies and in properties in Israel, and a diagram of the company's holdings in active companies and properties abroad as at December 31, 2005:

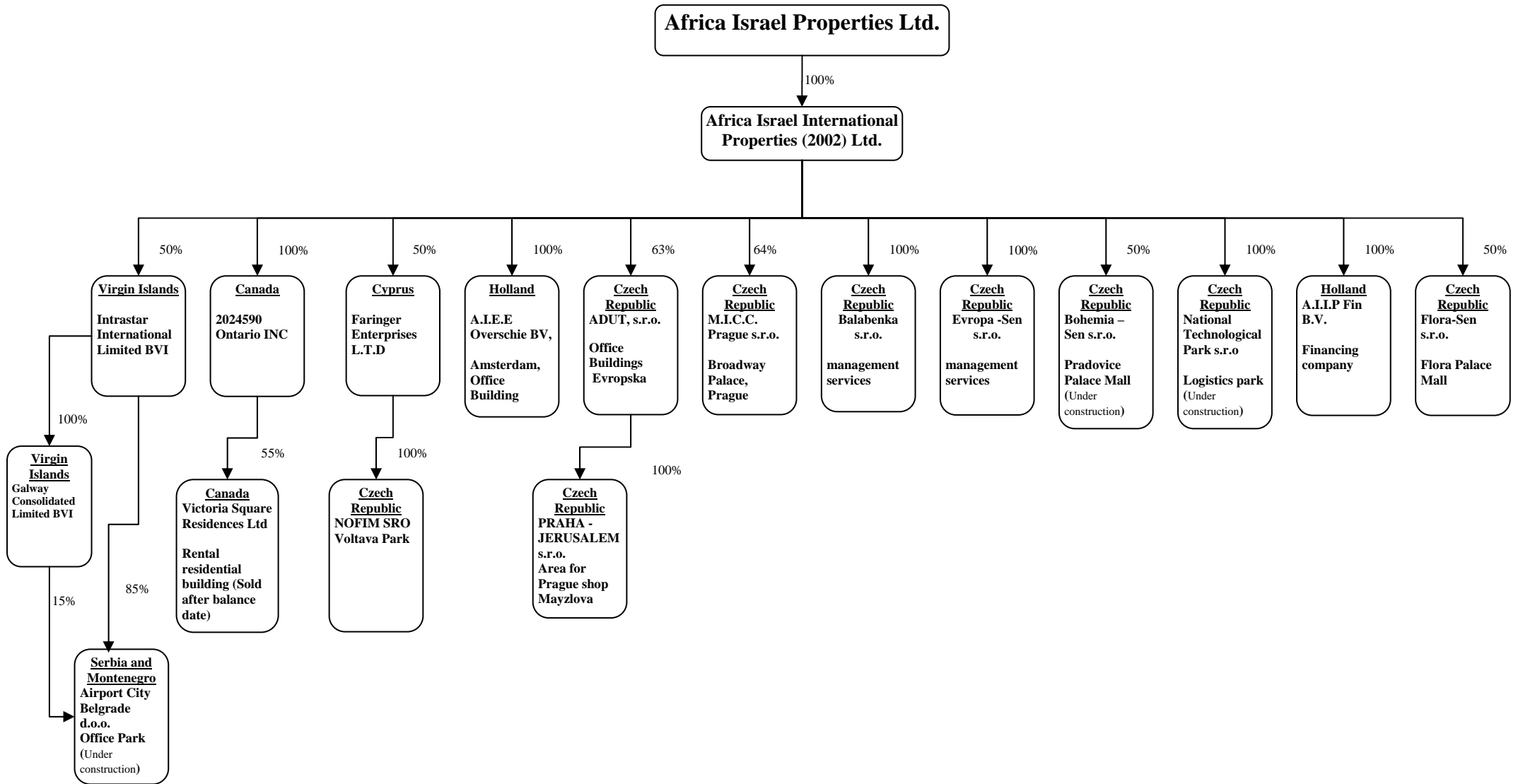
Diagram of the company's holdings in Israel



* Holding in Gush Helka company – Yefe Nof Haifa Development Company Ltd.

** Ramle, Gezer, Modi'in.

*** In March 2006 Bank Leumi Israel Ltd. exercised its right to sell to the Company, and to obligate the Company to purchase from it, all its shares in Af-Sar, namely 20% of the issued and paid up capital of Af-Sar. For details see 31 in the Financial Statements.



2. **FIELDS OF ACTIVITY**

The company's principal activities are initiating, constructing, renting and operating industrial, office and commercial buildings in Israel and abroad.

3. **INVESTMENTS IN THE CORPORATION'S CAPITAL AND TRANSACTIONS IN ITS SHARES**

3.1 During the year 2004, the company's registered capital was increased, and the structure of the registered capital was changed such that the company's total registered capital on December 31, 2005 is 20,000,000 ordinary, registered, shares of NIS 1 par value each.

Following is a table specifying the development of the company's issued and paid-up capital during the two last years:

Date	Nature of change	Number of shares	NIS par value each	Share class	Issued and paid-up capital in NIS
Balance on 31.12.03		115,996,229	0.001	Ordinary	About 115,998
		18,840	0.0001	Voting	
		1	0.001	Deferred	
11.8.04	Allotment to Africa Investments of a single voting share of NIS 0.001 par value each	1	0.0001	Voting	0.0001
11.8.04	Allotment of 9,999 voting shares, of NIS 0.0001 par value to Aframan Nominees Ltd.	9,999	0.0001	Voting	0.9999
11.8.04	Allotment to Africa Investments of 816 ordinary shares, of NIS 0.001 par value each	816	0.001	Ordinary	0.816

Date	Nature of change	Number of shares	NIS par value each	Share class	Issued and paid-up capital in NIS
11.8.04	<p>The structure of the company's issued and paid-up capital was changed as follows:</p> <p>In the first stage, the company's capital was consolidated and divided such that every 10 voting shares of NIS 0.0001 par value each were integrated and turned into a single voting share of NIS 0.001 par value each.</p> <p>In the second stage, the rights attached to the ordinary shares were changed and made parallel to the rights attached to the company's voting shares. Included in this change, and without limiting the generality of the above, was the granting of voting rights in the company's general meeting to the ordinary shares, voting rights of the kind attached to the voting shares. At the same time, the rights attached to the deferred shares were changed and made parallel to the company's ordinary, and voting, shares. Included in this change, and without limiting the generality of the above, was the granting of voting rights in the general meeting to the deferred shares - voting rights of the kind attached to the voting shares - as well as rights to the receipt of dividends parallel to the dividend receipt rights attached to the voting shares.</p> <p>In the third stage, the name of the shares included in the Company's share capital was changed in such a way that all the Company's shares shall henceforth be designated ordinary shares (all bearing in mind the absolute identity between the rights attaching to the ordinary shares, the voting shares and the deferred shares).</p> <p>In the fourth stage, the Company's share capital was consolidated and distributed in such a way that every 1,000 ordinary shares of NIS 0.001 n.v. were consolidated into one ordinary share of NIS 1. n.v.</p>				
13.9.04	Allotment to Africa Israel of 9,000 ordinary shares of NIS 1 par value each	9,000	1	Ordinary	9,000
13.9.04	Allotment of bonus shares	9,875,000	1	Ordinary	9,875,000
27.9.04	Issuance of shares to the public	2,000,000	1	Ordinary	2,000,000
29.12.05	Allotment of shares to Leumi and Co Investment House Ltd	631,579	1	Ordinary	631,579
Up to the date of this report	Exercise of option warrants (Series 1)	130	1	Ordinary	130
Up to the date of this report	Exercise of option warrants (Series B)	20,058	1	Ordinary	20,058
Total in NIS of issued and paid-up capital, as at the date of this report:					12,651,767

3.2 On September 13, 2004, the company's board of directors decided to approve a plan for the allotment of options to employees of the company or subsidiary of the company or the company's parent company (hereinafter - "**the plan**"). In addition to the approval of the company's board of directors, the plan also received the approval of the general meeting of the company. On December 13, 2004 (hereinafter - "**the determining date**") the company made an allotment under the plan, of 235,000 Option Warrants (hereinafter - "**the options**"), to 15 employees of Africa Investments who occupy positions in the company or who provide services to it, as well as to an employee of its subsidiary, convertible into 235,000 ordinary shares of NIS 1 par value each (subject to adjustments).

The period for exercising the options is as detailed below: one third of the amount of the options is exercisable commencing from the end of three years from the determining date; one further one third of the amount of the options is exercisable commencing from the end of four years from the determining date; and the balance totaling one third of the amount of the options, is exercisable commencing from the end of five years from the determining date. All the options are exercisable commencing from the date of commencement of the relevant option period and up to the end of six years from the determining date. The exercise premium of each option is 90% of the average stock exchange opening rate during the 30 trading days commencing with the date the company's shares were listed for trade on the stock exchange, and is linked to the Consumer Price Index (hereinafter - "**the exercise price**"). The exercise price shall only serve in determining the amount of the premium as detailed hereunder and will not actually be paid to the company. In the event of the options being exercised, the full amount of the exercise shares will not be issued, but only the quantity of shares which corresponds to the premium element of the exercised options.

Various adjustments were prescribed in the framework of the plan in cases of a distribution of bonus shares, an offer of securities by way of a rights issue and a dividend distribution. Following a distribution of a dividend to the company's shareholders (on December 19 and 20, 2005), the exercise prices were adjusted in respect of options that had been granted to employees as aforementioned in this section, to the extent that the amount of the dividend paid for each of the company's shares, was reduced. The adjusted exercise price will bear linkage differentials (according to the known index), from the "ex-dividend" date and until the exercise date (the exercise price will not under any circumstances, be reduced to less than the nominal value of each share). As at December 31, 2005 the exercise price of the said options stood at NIS 81.07 per share.

As of the date of the report 38,650 option warrants have expired as a result of the termination of the employment of two employees to the effect that they are no longer serving as employees of the company and/or the company's subsidiary and/or of the company's parent company.

3.3 On July 22, 2004, the company, Africa Investments and Bank Leumi, signed an options agreement, in relation to the acquisition of company shares. Within the framework of this agreement, the company granted Bank Leumi the option of acquiring a quantity of company shares, which would constitute 5% of any kind of means of control over the company (as defined in the 1968 Securities Law), after the allotment (hereinafter - "**the option agreement**"). On December 29, 2005 Bank Leumi assigned to Leumi and Co. Investment House Ltd. (above and hereinafter - "**Leumi and Co.**"), a wholly owned subsidiary of Bank Leumi, all its rights and obligations under the option agreement. Further to the foregoing and on the same day, notice of exercise of the option (which as aforementioned had been assigned by Bank Leumi), was received on behalf of Leumi and Co. Accordingly 631,579 of the company's ordinary shares were assigned to Leumi and Co., for a consideration of NIS 124.4 per share (a price which had been determined in accordance with the provisions of the option agreement and which reflects the average of the closing prices of the company's shares on every stock exchange trading day, during the 90 day period that preceded the exercise date), namely, a total amount of approximately NIS 78.6 million.

3.4 On September 27, 2004, the company issued to the public, by means of a prospectus, shares and convertible securities of the company, detailed as follows:

- a. 2,000,000 ordinary registered shares of NIS 1 par value each.
- b. 1,000,000 registered options (series 1) are exercisable for 1,000,000 of the company's ordinary shares each with a par value of NIS 1, on any trading day, commencing from the date of listing of the options for trading on the stock exchange and up to December 31, 2007 (inclusive), to the effect that each option (series 1) will be exercisable for 1 ordinary share with a par value of NIS 1, against payment of an exercise price of NIS 122.29 for each option (series 1), index linked, subject to adjustments. An option (series 1) that is not exercised by the expiration of the exercise period will expire, and the holders will have no right in it whatsoever.

The option (series 1) conversion rates which are specified in detail above in this section are after the making of an adjustment as a result of a distribution of dividend to the company's shareholders (on April 19 and on December 20 2005).

As part of the company's prospectus, Africa Investments undertook that on December 29, 2005 it would, during the course of trading on the stock exchange, offer to acquire all the options (series 1) at a price of NIS 20 for each option (series 1), linked to the Consumer Price Index. In accordance with such undertaking, on December 29, 2005, Africa Investments acquired 273,259 options (series 1) for a consideration of NIS 20.52 for each option (series 1). As at the date of this report Africa Investments holds 261,316 options (series 1).

After the date of the balance sheet and up to the date of this report 130 options (series 1) have been exercised for NIS 1 par value ordinary shares of the company.

- c. NIS 150,000,000 par value registered debentures (series b) of the company, repayable in four equal annual payments. The debentures are linked to the Consumer Price Index and bear interest at the rate of 4.65% per annum which is to be paid once annually. The debentures (series b) are linked (both principle and interest) to the rise in the Consumer Price Index and are convertible for NIS 1 ordinary shares of the company at par value, on any stock exchange trading day commencing from the date of their listing for trading and up to September 18 2009 (inclusive), except on the trading days that fall between September 19 and October 2 in each of the years 2006 to 2008 (inclusive), to the effect that in the period from the date of listing of the debentures and up to September 18 2006 all NIS 122.29 par value debentures are convertible for 1 NIS par value ordinary shares of the company and from September 19 2006 until September 18 2009, all NIS 136.4 par value debentures are convertible for 1 NIS par value shares of the company.

The aforementioned conversion rates in this section are updated in accordance with the adjustments made in the conversion rate as a result of distribution of a dividend to the company's shareholders (on April 19 and December 20 2005).

As aforementioned in section d hereunder up to the date of the balance sheet options (series 2) of the company have been exercised for 99,569,500 par value debentures (series b) of the company. As at December 31 2005, the balance of the debentures (series b) included in the turnover is NIS 249,569,500 par value.

From the date of the balance sheet and up to the date of this report, 2,452,893 par value debentures (series b) have been converted for 20,058 of the company's ordinary shares of NIS 1 par value.

- d. 1,000,000 registered options (series 2) convertible for NIS 100,000,000 debentures (series b) at par value on any trading commencing from the date of the listing of the options (series 2) for trading on the stock exchange and up to September 30 2005 (inclusive) except between the 12th to the 16th of every calendar month. Every option (series 2) shall be exercised for NIS 100 par value debentures (series b), against payment in cash of the exercise price of NIS 95, linked to the Consumer Price Index. By September 30 2005 995,695 options (series 2) had been exercised for NIS 99,569,500 par value debentures (series b). The remaining unexercised options (series b) have expired.

4. **DISTRIBUTION OF DIVIDENDS**

On 13th September 2004, the company's board of directors decided on a dividend policy according to which a dividend will be distributed, once in a calendar year, in the amount of 50% of the smaller of the two following sums: (a) the company's net income in the calendar year preceding the year on which the dividend is to be distributed; (b) the company's cash flow in the calendar year preceding the year on which the dividend is to be distributed.

What was said in the preceding paragraph is subject to the regulations of any law and especially to the existence of distributable profits, according to the provisions of the Companies Law, 1999, to keeping the company's commitments to third parties as they might from time to time be, to the requirements of the company's cash flow and its resources at any time, and subject also to the specific decisions of the company's board of directors regarding any distribution, and to any other decision the company's board of director might make at any time, including the assignation of the company's profits to another objective and changes of this policy.

On March 23 2005, the company's board of directors approved a distribution of a dividend in cash to the company's shareholders, out of the company's accumulated distributable profits, of a total sum of NIS 75 million. The dividend was distributed to the company's shareholders on April 19 2005.

On November 23 2005 the company's Board of Directors approved distribution of a dividend in cash to the company's shareholders out of the company's accumulated distributable profits, of a total sum of NIS 40 million, the dividend was distributed to the company's shareholders on December 20 2005.

5. **FINANCIAL INFORMATION REGARDING THE CORPORATION'S ACTIVITIES**

For financial information regarding the company's activities, see the company's financial statements as at December 31, 2005, attached hereto (hereinafter - "**the financial statements**").

6. **THE GENERAL ENVIRONMENT AND THE IMPACT OF EXTERNAL FACTORS ON THE CORPORATION'S ACTIVITIES.**

What is said in this section is based on the trends, events and developments in the company group's macro-economic environment which have or are expected to have an effect on the company's business results. For this reason, any reference made in this section to the company's evaluation of the anticipated developments and to their effect on the company group, is to be regarded as prospective information, which is beyond the company's control and is uncertain.

6.1 **Market and sector effects.**

The company group is exposed to changes in the conditions of the income-generating real estate market in Israel and in the countries in which it is active. As at the date of this report, the company's principal activity abroad is in Eastern Europe.

6.1.1 **Condition of the income-generating real estate market in Israel**

2005 has all the indications of a year of change in the income-generating real estate market in Israel. The improvement in the economic situation, tranquility in the renewed growth in the economy together with the new regulations making it possible for the establishment of income-generating real estate investment funds (REIT) commencing from the beginning of 2006, has caused a revival in activity in this sector. Correspondingly, in view of the reduction in the number of building starts in the sector and in view of the improvement in the economic situation, as above mentioned, a reduction has occurred in the availability of vacant office space for letting and there has accordingly been a trend of a rise in office rents (mainly in the areas of demand). The above state of the income-generating real estate market in Israel has brought about a situation in which the occupancy in the office space of the company group and in areas designated for high tech industry, commencing from 2005, is on the increase and is accompanied by a trend of rising prices in new lettings as opposed to the prices that prevailed between 2002 and 2004. The improvement in the economic situation has raised the percentage turnover of shops in the commercial areas of the company group and an increase in prices is indicated upon renewal of some of the contracts in shopping malls that it owns.

The improvement in the state of the market is expected to continue in the short term. It is nevertheless difficult to estimate the long term trend, *inter alia*, in view of the impact on the state of the market, of the political and diplomatic situation in Israel.

6.1.2 **The state of the market in the income-generating real estate market in Eastern Europe**

The Czech Republic

Czech economic growth (growth in the gross domestic product) is expected, in 2005, to amount to approximately 4.9% as opposed to approximately 4.4% in 2004. This growth trend, as well as a continuation in the reduction in the number of unemployed (8.9% in 2005 as opposed to a rate of 10.2% in 2004) point to an improvement in the Czech economy stemming *inter alia* from continued foreign investment in the Czech Republic.

Office space for rental increased in 2005 by approximately 14% as opposed to the available office space in 2004. Nevertheless, no material growth has been recorded in the amount of vacant space. This, in the company's estimation, indicates a trend of stability in the market in office space in Prague.

Czech economic growth and the entry of new international retail chains have, in 2005, created a demand for further commercial areas in Prague. In 2005 three new shopping centers were opened in Prague located in the suburbs. In 2006 it is anticipated that a further

three shopping centers will be opened. The urban demand and a continuation of the growth trend of the Czech economy have a positive impact on the growth of demand for storage space and logistics.

Serbia

The Serbian economy is continuing the process of recovery that has characterized it since the end of the war. The office lettings market in Belgrade has in recent years been characterized by a movement from offices located in residential premises to modern office buildings that are not located in the city center.

Romania

The Romanian economy in recent years is characterized by a substantial growth in urban demand principally in the field of private consumption a shortage in commercial areas exists which has been expressed in a number of enterprises for the establishment of shopping malls in the capital Bucharest.

6.2 Fluctuations in foreign currency rates

Financial statements of non-Israeli members of the company group are made in foreign currency: Canadian dollars, Euro and Czech Crowns. For the changes in foreign currencies exchange rates see Note 2 (n) to the financial statements.

For the effect of the changes in foreign currency exchange rates see Note 2 (n) to the financial statements.

6.3 Changes in the Consumer Price Index

For the rate of change in the CPI see Explanation 2 (n) to the financial statements. The rate of change in the Israeli CPI affects the company's financing expenses (because of CPI linked credit), as well as the company's earnings from the rents paid, which are mostly CPI linked.

6.4 Changes in legislation and accountancy standardization

For changes in legislation and book-keeping standardization and their effect on the company group see Notes 2 (s), 2 (t) and 2 (u) to the financial statements.

It should be pointed out that the above factors might have an impact on the business activities of the company group and on its financial results, for better or for worse, according to their trends, in the future as well. The degree of such an impact, if any, depends, inter alia, on the intensity of the events, their extent, their duration, and the company's ability to confront them.

CHAPTER 2 – DESCRIPTION OF THE CORPORATION'S BUSINESS

7. GENERAL INFORMATION

The company is active in the field of income-generating real estate since its foundation in 1971. The company group owns buildings used for industry, commerce and offices in Israel and abroad. In addition, the company group has assets in construction, land and building rights which are as yet unused.

The information in this chapter is a description at group level and therefore wherever the expression "the company" appears it also means that company through its investee companies.

7.1 Structure of the field of activity and the changes taking place in it

The sector of income-generating real estate in Israel and abroad includes the initiation, planning, construction, marketing and operation of rental properties, designated mostly for industry, commerce, office space, residence, car-parks, storage and logistics.

7.2 Limitations on the field of activity imposed by legislation, standardization and special constraints

As said above, the main part of the field of activity of the company group consists of real estate properties. Consequently, legislation regarding real estate and municipal taxation, including purchase tax, sale tax, betterment levies imposed on real estate transactions, affect its activity. In addition, the municipal property rate also affects the company's field of activity.

7.3 Changes in the extent and profitability of activity in the field

As said in section 6.1.1 above, 2005 was characterized *inter alia* by a fall in supply of surplus vacant rental spaces in office buildings and in industrial parks in Israel, this in view of the improvement during the said period in the economic situation and in view of the reduction in the number of building starts of these kind of projects.

7.4 Crucial success factors in the field of activity

The crucial success factors in the company group's field of activity are mostly the location of the property, and knowledge and experience in locating and exploiting business opportunities, in planning, construction, marketing and operation of properties.

7.5 Entrance and exit barriers

There are no formal entry and exit barriers in this field of activity. At the same time, considering the special nature of this field of activity, financial solidity and access to financial resources are necessary. In addition, knowledge of, and experience in, the crucial success factors in this field of activity (mentioned in sub-section 7.4 above), are also required. Leaving this field is not a move which allows flexibility, since the possibility of realizing the properties is dependent on, *inter alia*, their location, their physical condition and the state of the market. Furthermore, realizing the properties involves various costs, including real estate taxation costs.

7.6 The structure of competition in the field of activity and its recent changes

Most of the competition in the sector is affected by the geographical location of the property. Most of the company group properties have in their vicinity competing similar properties. In addition, competition

revolves around rent rates, the physical conditions of the buildings, the finish standards of the properties and the quality of management services given to the lessees.

8. **PRODUCTS AND SERVICES**

The company group's products are mainly rentals of office, industrial and commercial spaces. For detailed information on the company group's properties in Israel and abroad, including the company group's earnings from renting and operating these properties, and their rate of occupancy, see section 13 below.

- 8.1 **Offices in Israel** - The most important office building of the company group in Israel are: Africa Israel Tower (Migdal Africa Israel) in Tel Aviv; Hakiryat Tower (Government Campus Tower) in Tel Aviv; the office building above the Ramat Aviv mall; Concord Towers in Benei Brak; and office spaces above the Savyonim mall in Yahud.
- 8.2 **Industry and science parks in Israel** - The company group owns industry and science parks, among which are Kiryat Weizmann – Ness Ziona Science Park, Kiryat Hamada in Migdal Ha'emek; Global Park in Lod; and Rehovot Park.
- 8.3 **Commerce in Israel** - The company group owns malls and other commercial spaces in Israel, the most important of which are: the Ramat Aviv Mall in Tel Aviv and the Savyonim Mall in Yahud.
- 8.4 **Offices, commercial and logistics abroad** - The company group owns a number of properties abroad, the most important of which is the Palace Flora Mall in Prague, in the Czech Republic. The company group also owns other office and commercial spaces in the Czech Republic, Holland, 50% of the rights to a plot in Bucharest - Romania in which it is planned to build, *inter alia*, a shopping mall (see Note 4.d (6) to the financial statements) as well as additional projects under construction (commercial, office, logistics and other areas) in Belgrade - Serbia and in Prague. After the date of the balance sheet the company also commenced operating in Manila in the Philippines where it has acquired shares in a company that owns the right in a park in which there are office buildings and additional building rights (see Note 31 to the financial statement).
- 8.5 **Others** - In addition to the company group activities specified above:
- a. The company holds, through a Canadian subsidiary in which the company holds (indirectly) approximately 55% of the share capital, a rental apartment building in Toronto, Canada. After the date of the balance sheet the company group entered into the contract for the sale of the aforementioned building.
 - b. The company group is building student dormitories on Mount Scopus in Jerusalem under the B.O.T. method.

9. **SEGMENTATION OF EARNINGS AND PRODUCTS PROFITABILITY**

	Rental space as at Dec. 31, 2005 (sq. m.)	Rate of occupancy as at Dec. 31, 2005	Company Group Income for 2005 (in NIS thousands)	Percent of total company group earnings
Science and industry parks in Israel	121,769	91.8%	54,110	23.1%
Offices in Israel	55,243	97.9%	49,105	21%
Commerce in Israel	27,372	100%	88,891	37.9%
Office, commerce and residence abroad	49,848	87%	42,147	18%
Total	254,232	93%	234,163	

	Company Group Income for 2004 (in NIS thousands)	Percent of total company group earnings for 2004
Science and industry parks in Israel	53,385	23%
Offices in Israel	29,239	12.6%
Commerce in Israel	83,780	36.1%
Office, commerce and residence abroad	65,558	28.3%
Total	231,962	

The proportion of the gross income (i.e. earnings of the company group from rent and operation of properties, after deduction of properties operation and maintenance, and of amortization and depreciations):

- in 2005 amounted to about 66.2% of its total earnings; the gross income of the company group amounts to NIS 155.1 million.

- in 2004 amounted to about 65.6% of the total income, and the amount of the gross earnings of the company group amounted to NIS 152.4 thousands.

As stated above, in December 2002 the company acquired the main income-generating real estate properties of the Africa Investments Group abroad and in December 2003 the main income-generating real estate properties of Africa Investments Group in Israel were transferred to it with a consequential segmentation in the revenues and profits in 2003 and moreover the rate of gross earnings in 2003 are not comparable in relation to segmentation in 2004 and 2005.

10. **Clients**

The company group has over 500 clients, who rent spaces of varying dimensions. As at the date of the balance, the company group has no client whose rent amounts to 10% or more than the company group's earnings from rent.

Doubtful debts – the company directorship examines regularly the nature of the clients, in order to determine the amount of allowance for doubtful debts. For details regarding doubtful debts see Note 7 to the financial statements.

11. **Marketing and promotion**

The company group works in diverse methods of marketing and *inter alia* as detailed below as follows:

- a. Marketing through marketing personnel who are employees of the company group and employees of Africa Investments.
- b. Contracting from time to time – with independent marketing firms and their international real estate agencies as a rule, exclusivity is not granted.
- c. Publication of information concerning the group's properties in the national and local press and in the company's internet site.
- d. Approach by direct mailing and by advertising campaigns in the various mass media, aimed attracting people to the company group's malls.

12. **Competition**

Competition in the field of income-generating properties takes place, mostly, in the zone in question. This means that in effect, in almost every site where the company group holds rental spaces, other companies who also own rental spaces in that area which they want to let – generally for the same purpose – compete with the company group.

The income-generating properties markets in Israel and abroad abound with competitors. Listed below are the main competitors of the company group, in relation to its most important properties:

- a. Ramat Aviv Mall – the mall competes with a number of malls in the Tel Aviv metropolitan area. Among these are the Seven Stars Mall, the Arena Mall in Herzelia, Ayalon Mall in Ramat Gan, Azrieli Mall in Tel Aviv, and Givatayim Mall.
- b. The Kiryat Weizmann Ness Ziona Science Park – the park competes with other, similar and adjacent, parks, such as Tamar Park, as well as with other similar parks in Israel's central region.
- c. Africa Israel Tower in Tel Aviv, spaces designated for free renting in the Kirya Tower in Tel Aviv, and Concorde Towers in Bnei Brak, all compete with similar built areas in the Tel Aviv metropolitan area in general, and especially in the areas of the City of Tel Aviv, of Ramat Gan and of Bnei Brak.
- d. Palace Flora Mall in Prague – the mall competes with other Prague malls.

The company group competes with the said local competition by, among other means, ensuring a regularly high standard of maintenance and management of its properties, while building up and preserving the company group's reputation in this respect. In addition, the company group uses various marketing methods in order to emphasize the advantages of its properties in comparison with its competitors' properties.

The company is unable to estimate the company group share of the market in relation to this field of activity.

13. Fixed assets

Following is concentrated data on lands and building rights belonging to the company group, as yet unused:¹

Project\property name	Project\ property concessionaire	Company's share of project\ property	Unused building Rights (in sq. m.)	Cost of property as on 31.12.2005 (in NIS Thousands)
Africa Israel Tower - Tel Aviv, additional floors	The company	66.66%	approx 4,000	11,900
Concorde Towers - Bnei Brak, Stage B	The company	63%	approx 12,982	46,532
Building rights in the Science Park - Ness Ziona	The company	100%	approx 4,590	-
An empty lot adjacent to the Science Park - Ness Ziona	The company	100%	approx 75,758	7,870
An empty lot in Global Park – Lod	Af-Sar Ltd.	80%	No building rights	3,029
RGM (Ramle, Gezer, Modi'in)	The company	60% / 50%	building rights not yet approved	444
Voltava Park - Prague, Czech Republic ²	Nofim Czech Republic s.r.o	50%	approx 37,000	33,153
Airport City Belgrade - Serbia -Stage 2 ³	Airport City Belgrade	50%	approx 107,000	19,390
Logistic Warehouses - Czech Republic	National Technological Park s.r.o	100%	approx 90,000	28,823
Total				151,141

¹ The data in this table regarding properties owned by the company is shown according to the company's relative share in these properties. Data regarding properties owned by subsidiaries is shown as "100%".

² The data being shown is as per 100%, as the company which holds this property is a fully consolidated company.

³ The data being shown is as per 100%, as the company which holds this property is a fully consolidated company.

The information detailed below concerns buildings for letting of the company group that are in the planning and construction stages:

Name of the Project/Property	Project/Property Concessionaire	Area under Construction (in square meters)	Stage reached at December 31, 2005	Expected finishing Date (estimation)	Balance of Cost at December 31, 2005 (NIS thousands)	Anticipated Balance of Costs. (in NIS Thousands)
The Kirya Tower-Tel Aviv - Stage B	One Half Jubilee Ltd.	29,000	Finishing works	Second quarter of 2006	61,707	40,000
Building at 6, Herzl Street, Tel Aviv	The Company	approx 1,700	Finishing works	April 2006	Costs included in Africa Israel Tower in Tel Aviv	100
The Students dormitories at Mount Scopus in Jerusalem	One Half Jubilee Ltd.	1,629 beds	Under Construction	2006 - 2008	28,498	50,000
Pradovice Mall in the Czech Republic	Bohemia - Sen s.r.o.	50,000	Planning	2008	4,335	160,000
Airport City Belgrade - Serbia - Stage A	Airport City Belgrade d.o.o.	18,000	Under Construction	2006	72,133	51,000
Total					166,673	301,100

The following table presents concentrated data on the income-generating properties of the company group, (not including properties of affiliated companies), as on December 31, 2005:

Company held properties								
Property name And location		Rental area in sq. m.	Occupancy in % On December 31		Earnings from rent and operation of properties (in NIS thousands) In the year		Cost of property as at December 31, 2005 In NIS thousands	
			2005	2004	2005	2004	Total cost ⁴	Reduced cost ⁵
1.	Buildings in Ness Ziona Science park	45,580	97%	95%	23,480	26,104	214,683	119,421
2.	Business Park In Rehovot	15,058	70%	100%	3,482	3,606	64,992	61,117
3.	Concorde Towers in Bnei Brak	8,018	89%	86%	5,531	4,888	83,604	69,511
4.	Atarim Car Park In Tel Aviv – sold 9.05	-	-	-	299	448	-	-
5.	Panorama Center In Haifa	-	-	-	329	380	6,284	5,075
6.	Savyonim Mall in Yahud – offices	4,892	100%	100%	3,353	3,229	111,973	92,154
7.	Savyonim Mall in Yahud – mall	6,340	100%	100%	12,599	12,114	Included in section 6 of this table	Included in section 6 of this table
8.	Africa Israel Tower in Tel Aviv	8,662	100%	98%	9,522	9,765	153,618	141,662
9.	Africa Israel House in Yehud	2,600	93%	68%	1,782	1,767	17,378	15,483
Total for company held properties		91,150	-	-	60,377	62,301	652,532	504,423

⁴ Cost of land and building after deduction of grants, including financing, management and general costs, which were capitalized for the buildings during the construction period.

⁵ Cost after reduction of grants and of amortization.

Properties held by subsidiaries in Israel								
Property name And location		Rental area in sq. m.	Occupancy in % On December 31		Earnings from rent and operation of properties (in NIS thousands)		Cost of property as at December 31, 2005 (In NIS thousands)	
			2005	2004	2005	2004	Total cost ⁶	Reduced cost ⁷
10.	Buildings in Ness Ziona Science park	31,322	96%	86%	14,907	14,094	143,133	110,928
11.	Global Park, Lod	21,393	88%	83%	9,669	7,139	107,580	98,603
12.	Global Park, Lod	1,600	100%	100%	2,054	1,484	23,947	20,523
13.	Buildings in Kiryat Hamada in Migdal Ha'emek .	8,416	98%	99%	2,572	2,442	21,194	17,033
14.	Ramat Aviv shopping mall site – offices	9,673	100%	100%	9,276	9,142	379,706	302,003
15.	Ramat Aviv shopping mall site - mall	17,849	100%	100%	61,951	59,621	Included in section 14 of this table	Included in section 14 of this table
16.	Ramat Aviv shopping mall site – car park	-	-	-	10,650	10,181	Included in section 14 of this table	Included in section 14 of this table
17.	Hakirya Tower- Stage 1 ⁸	22,981	99%	-	20,560	-	260,053	257,100
Total for properties held by subsidiaries in Israel		113, 234			131,639	104,103	935, ,613	806,190

⁶ Cost of land and building after deduction of grants, including financing, management and general costs, which were capitalized for the buildings during the construction period.

⁷ Cost after reduction of grants and of amortization.

⁸ Stage 1 of the Kirya Tower, is shown pro- rata to the Company's share in it (50%).

Properties held abroad								
Property name And location		Rental area in sq. m.	Occupancy in % On December 31		Earnings from rent and operation of properties (in NIS thousands)		Cost of property as at December 31, 2005 (In NIS thousands)	
			2005	2004	2005	2004	Total cost ⁹	Reduced cost ¹⁰
18	Maiselova, Prague	1,060	17%	17%	313	177	2,701	1,934
19	Broadway Palace, Prague – offices	6,386	52%	100%	1,110	8,104	57,875	49,607
20	Broadway Palace, Prague – commerce	2,830	95%	100%	4,573	6,744	Included in section 19 of this table	Included in section 19 of this table
21	Evropska , Prague	4,742	100%	95%	4,243	4,077	34,302	28,899
22	Palace Flora, Prague – mall ¹¹	10,235	100%	100%	18,578	34,374	206,101	194,200
23	Palace Flora, Prague – offices ¹²	8,795	98%	72%	6,601	7,468	Included in section 22 of this table	Included in section 22 of this table
24	Mod Village Toronto - sold 1.05	-	-	63%	-	1,822	-	-
25	Victoria Square Toronto	13,000	89%	-	4,069	-	122,450	121,630
26	Overschie, Amsterdam	2,800	79%	84%	2,660	2,792	38,686	35,075
Total for abroad		49,848	-	-	42,147	65,558	462,115	431,345

Total	254,232				234,163	231,962	2,050,260	1,741,958
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⁹ Cost of land and building after deduction of grants, including financing, management and general costs, which were capitalized for the buildings during the construction period.

¹⁰ Cost after reduction of grants and of amortization.

¹¹ Flora Palace, is shown in 2005 pro rata to the Company's share in it (50%) and in 2004 at 100%.

¹² Flora Palace, is shown in 2005 pro rata to the Company's share in it (50%) and in 2004 at 100%.

For more information concerning the company group's fixed assets, see Note 3 to the financial statements

As regards sale and acquisition of assets after the date of the balance sheet see Note 31 to the financial statements.

The data presented in above tables includes prospective information. Prospective information cannot be taken as certain as far as it relates to the future. It is based on information possessed by company at the time this report was written. The tables also contain the company's estimates or intentions, as they stood at the time this report was written. The prospective information is based on the company's evaluations, which take into account, inter alia, past experience (and on the information provided for it by companies in the company group). Actual results could be materially different from the estimates specified above and from what they imply for various reasons (some of which are not within the company's knowledge at the date of this report) such as delayed approvals from the relevant authorities, obstacles that the contractors connected to the company group might face, etc.

14. **Intangible assets**

In accordance with the agreement on the use of a trademark, signed between the company and Africa Investments in September 2004, the company was granted the right to use the trademarks of Africa Investments (hereinafter: "**the trademark**"). In keeping with this agreement, the company was granted the right to use the trademarks without any limitation of time and for no consideration when the company acts in pursuit of its business in its fields of activity, for as long as Africa Investments holds 50% or more of the voting rights at the company's general meeting. The trademarks were defined as the trademarks associated with the logo of Africa Investments, which were registered in the fields of activity of Africa Investments at the date of the listing of the company's shares for trade on the Tel Aviv Stock Exchange (October 2004).

15. **Human capital**

15.1 On July 27th 2004 an agreement was signed between the company of the first part and Africa Investments of the second part in which it was provided that Africa Investments would provide to the company, by itself or through its subsidiaries, management, consulting and supervisory services in relation to company group, this being in return for the payment of management fees. It was provided that the said agreement would be in force commencing from January 1 2004 for a term of two years and it would be automatically renewed for a further year at the end of each calendar year unless either of the parties notified otherwise. The management fees also include payment in consideration for the provision of management services to some of the company's subsidiaries. For a detailed outline of this agreement see section 21.2 below.

The total of amount of management fees that the company group paid Africa Investments in 2004 amounts to NIS 17,669 thousands and NIS 9,341 thousands in 2005.

15.2 It was furthermore provided in the agreement that the company would pay Africa Investments, in addition to the aforementioned management fees, the full cost of the

salaries, including provision made in respect of termination of employment contingencies, of Africa Israel employees actually engaged in the marketing of and holding of the aforementioned properties of the company group (in this subsection hereinafter - "**the transferred employees**"), details of whose functions and salary costs are set forth in the management agreement. This arrangement was automatically terminated at the end of 2004 in accordance with the provisions of the management agreement.

- 15.3 In accordance with an addendum to the management agreement of August 29, 2004, the transferred employees were transferred to the company commencing from January 1, 2005 so that with effect from January 2005, these employees are direct employees of the company.
- 15.4 The company has 54 employees in Israel, most of who are engaged at the various sites that the company operates, as well as 36 employees overseas, principally in the company's headquarters in Prague.
- 15.5 There are 4 office bearers in the company, detailed hereafter as follows: its Director General, Vice-Director General for Finance, Internal Auditor and the Company Secretary. The services provides by the office bearers are included within the framework of the management services that are governed by the management agreement between the company and Africa Investments.

16. **Working capital**

- 16.1 In the company's line of work, terms of payment are determined within the framework of the lease agreements signed by the leasers and the company group. Leasers usually pay in advance for a period of one month, two months, a quarter of, or an entire, year.
- 16.2 The ratio of the working capital as at December 31, 2005, reached 1.4 (in comparison with 1.36 as at December 31, 2004).

17. Investments

Following is a table which summarizes the company's investments in affiliated companies (in NIS thousands):

Held company	Holding in %	Total investment in the company, In the consolidated report for 31.12.2005	Property name
Machzevot Haifa Ltd.	45%	18,265	Lev Hamoshava in City Center, Haifa
Joint Transaction, Lev Talpyot	40%	3,706	Kanyon Lev Talpyot, Jerusalem
Total		21,971	

18. Financing

18.1 During the period of the report the company financed its activities from shareholders capital, by a loan raised from institutional investors in the framework of the issue of bonds (Series A) on February 5, 2004, as well as from debentures (Series B) issued through a prospectus that the company published in September 2004, in accordance with which the company issued shares, convertible bonds and share options. The company's activity is also financed by bank credit to be used in the acquisition or construction of income-generating properties in Israel.

The company's subsidiaries finance their activities by credit extended by the company, and by bank credit to be used for the acquisition or construction of income-generating properties in Israel and abroad.

18.2 On September 13, 2004, an agreement was signed between the company and Africa Israel Finance (1985) Ltd. which governs the day to day financing activity between them. For details relating to this agreement see Section 21.1 hereunder.

18.3 The company may at any time deposit with Africa Finance, a sum of not exceeding 35% of its shareholders' equity and Africa Finance may at any time deposit with the company, a sum of not exceeding 100% of the amount of the company's capital.

As at December 31, 2005 the balance of the amount deposited by the company in Africa Finance stood at NIS 271,943 thousands.

The balance of the company's deposit in Africa Finance as at December 31, 2005, after deduction of the balance of the company's debt to Africa Finance as at December 31, 2005 (which amounted to NIS 77,851 thousands) amounts to NIS 194,092, constituting approximately 20% of the company's shareholders' equity as at December 31, 2005.

On January 29, 2006 the company deposited NIS 380 Million with Africa Finance under the terms of the financing agreement.

18.4 On April 1 1995, Africa Investments issued to the company a capital bill of the sum of NIS 40 million. This capital bill is not linked to the CPI, does not bear interest, and is not designated for settlement.

18.5 As of December 31 and the date of this report, any bank credit received by the company group is credit designated for financing of construction and acquisition of company group properties. In addition to the aforementioned bank credit, the company issued in 2004 two series of long term bonds (linked to the CPI), in the total sum of about NIS 511 millions (including debentures (Series B) of the company) arising from the exercise of the company's option warrants (series 2)). The average interest on these bonds is 5.1%. As regards the estimated balance of the bonds and details concerning dates of repayment of the bonds, see Notes 15 and 16 to the financial statements

For details regarding the financial criteria, see Note 26(D) to the financial statements.

18.6 From December 31, 2005 and up to the date of this report, the company group took no credit of any significant amount.

The company group was provided with credit lines designated for the completion of the Migdal Hakiryia project, in construction of the Students Dormitories in Jerusalem, and the construction of Stage 1 of the Airport City Project in Belgrade. The company group has no general credit line.

18.7 See Notes 13, 14, 17 and 19 to the financial statements, for the composition of the credit taken by the company group, and the interest rates paid for it. As specifically explained in these notes, part of the interest for this credit is variable in keeping with the changes in the LIBOR interest, the Eurobor and the prime on the Canadian dollar. From December 31, 2005 and up to the date of this periodic report, no significant changes have occurred in the aforementioned interest rates.

18.8 As regards the impact of limitations on the indebtedness of a group of borrowers (pursuant to the Bank of Israel's Correct Banking Management Regulations), see Section 20 hereunder.

19. **Taxation**

19.1 The company received assessments from the income tax authorities for the years 2000, 2001 and 2002, according to which the company ought to pay the sum of about NIS 5.2 millions (not including interest and linkage differentials), mainly because part of the company's financing costs were disallowed. The company's management rejects the demand of the tax authorities and had appealed to the District Court against these assessments. According to the opinion of its legal advisers, the company believes that its objections stand a good chance of being accepted, and for this reason no allowance was included in the financial statements in respect of this demand. Except as aforementioned, the company has final assessments up to and including the 2002 tax year. Likewise, some

of the incorporated companies have final assessments up to 2002, and for others, final tax assessments have not been issued since the start of their activities.

- 19.2 The income tax rate imposed on the company and on the incorporated companies in Israel in 2005 is 34%.

The tax rate on capital gains is 25%. (The rate of tax on a capital gain made prior to January 1, 2003, the rate of corporation tax and the rate of tax on capital gain made after January 1, 2003, is 25%. The tax liability is calculated linearly.)

- 19.3 In October 2003, the company and Africa Investments signed an agreement with the Income Tax Commission, regarding the transfer of assets and stock owned by Africa Investments to the ownership of the company, as part of the re-organization process and concentration of the income-generating real estate activities.

The transfer was made in accordance with Section 104 A of the Income Tax Ordinance.

- 19.4 In March 2002, the Knesset approved Amendment No. 50 to the Real Estate Taxation Law (Improvement, Sale and Acquisition), 1963, (hereinafter in this section: "**the amendment**"), which came into force on 7 November 2001 (hereinafter in this subsection: "**the commencement day**").

The amendment provides, inter alia, that a company, selling a right in real estate or in activity in a real estate corporation, will bear corporation tax on the real improvement created until the commencement day and a 25% tax rate on the improvement created since the commencement day. The amendment also establishes reductions in betterment tax for real estate transactions made during the years 2002 and 2003, and exemptions from sales tax for residential apartments and real estate properties acquired after the commencement day.

- 19.5 On 24 July 2002, the Knesset approved the Amendment of the Income Tax Ordinance (Amendment No. 132), 2002 (hereinafter in this section: "**the tax reform**"), applicable from 1 January 2003 onward. The basis of taxation in Israel was amended within the framework of the tax reform so as to make it personal rather than territorial\geographic. Since 1 January 2003, Israeli citizens are to be taxed on a world-wide basis, on their total income.

The main tax reform regulations that can affect Israeli companies are:

- a. Rules of origin – rules were established to determine where the production of the income originated.
- b. Controlled foreign company (CFC) – rules were established according to which in certain cases Israeli stock owners are liable to taxation on notional dividends, for passive income from a foreign country-based company, which they control.
- c. Offsetting losses abroad – limitations were set on the possibilities of offsetting losses incurred abroad.

- d. Tax credit - special tax credit regulations were established, intended for Israeli residents who had paid foreign taxes on incomes originating abroad.
- e. Capital gain – the tax rate on capital gain was reduced from the rate of corporation tax to 25% with the exception of a capital gain on marketable securities for a company, in the Adjustments Law. The "Seven Years Limit" for use of transferred capital loss was annulled. (Applicable to losses made in the tax year 1996 and onward).
- f. Transfer costs – a general directive was established, enabling intervention in the setting of prices and conditions in international transactions made between associated parties, to be applied when regulations on this subject are prescribed. (No such regulations have yet been made).

19.6 In December 2002, Africa Israel acquired International Properties (2002) Ltd, (a company wholly owned by the company), from foreign corporations held by Africa Investments, holdings of the Africa Investments group in properties located in the Czech Republic, in Holland, and in England.

To the best of the company's knowledge, on December 31, 2003 Africa Investments signed an agreement with the Income Tax Commission, regarding taxation of the profits accumulated in the above companies up until December 31, 2002, and regarding changes in the organizational structure, as a result of the tax reform. Africa Investments paid for these profits a one-time tax at the rate of 5% (5,382 NIS thousands).

As a result of this transfer, the cost in the books of the said companies' stock is lower than the acquisition value which will be taken into account for the purpose of tax calculation for such a sale, at the time these companies are sold (if sold), so that the company will not be charged with tax for the gains accumulated in the said companies up to the date of their acquisition by the company.

19.7 The tax rates which fall on companies in the various countries where the group members operate are as follows:

-	The Czech Republic	in 2005 – 26%, from 2006 onwards – 24%.
-	Canada	35%
-	Holland	31%
-	Serbia	10%
	Romania	16%

19.8 On July 25, 2005, the Knesset approved an Amendment of the Income Tax Ordinance (Amendment 147 and Temporary Provision), 5765-2005, (hereinafter in this subsection- "**the amendment**"). The amendment establishes a gradual reduction of corporation tax in the following way: in the 2006 tax year a tax rate of 31% will apply, in the 2007 tax year the tax rate will be 29%, in 2008 the tax rate will be 27%, in 2009 the tax rate will be 26% and from the year 2010 onwards, the tax rate will be 25% with a reduction in the rate of corporation tax to 25%, every capital gain in real terms will be taxable at rate of 25%.

The current taxes and the balances of the deferred taxes as at December 31, 2005, in respect of the companies operating in Israel, are calculated in accordance with the new tax rates, as prescribed in the amendment. The effect of these changes on the consolidated financial statements for 2005 is a reduction of the expenditure on income taxes which amounts to about NIS 6.5 million.

19.9 Concerning the existence of accumulated losses, and the sums of deferred taxes acknowledged for them, see Note 25 to the financial statements.

For the difference between effective tax rate and the rate of the theoretical tax rate, which fall on the company, see Note 25 to the financial statements.

For additional details regarding taxation of the company group incomes, see Note 25 to the financial statements.

20. **Limitations on corporation activities and their supervision**

The company's activities are subject to laws – both by way of legislation and by way of standardization of planning, construction and renting.

The planning and construction law (including regulation prescribed thereon) regulate the company's activities in every things connected with receipt of building permits, site safety during construction, occupancy permits, as well as business licensing when required.

At the end of each project, approbations of the authorities in charge, such as the Standards Institute, the Fire Brigade, and others, must be obtained.

As said above in this report part of the company's properties were transferred to it at the end of the year 2003, in accordance with section 104 of the Income Tax Ordinance. The limitation that had existed, as part of compliance with the condition imposed in the section, on the sale of the said properties within a period of two years, ended on December 31, 2005.

Group borrower indebtedness limitations – the Africa Investments group of companies constitutes a "group of borrowers" (as the term is defined in the correct banking procedure regulations of the Bank of Israel in relation to limitations on indebtedness of a single borrower and of a group of borrowers (hereinafter - "the procedure")). As a result, Israeli banks are limited in the maximum amount of credit they are allowed to place at the disposal of any one of the Africa Investments companies group and the company included, determined by the overall amount of the credit placed at the disposal of the group and of the person who controls it.

Africa Investments and Alon Israel Oil Company Ltd. (hereinafter - "**Alon**") have been notified recently by representatives of two banks that in view of the rights of Africa Investments in Alon for preventing the adoption of various decisions in Alon and in its subsidiaries, and in light of the definition of the term "control" contained in the procedure, Africa Investments Group and Alon Group must be viewed as one group borrower for the purposes of the procedure. As a consequence of this, these banks are precluded from making additional credit available to the companies comprised in these two groups. Africa Investments has made an approach to the

Inspector of Banks in a application setting out reasons in detail, to the effect that in the circumstances of the case, this is an instance in which it would be appropriate for the Inspector to exercise the power vested in him in the procedure and issue a directive as to the detachment of the Alon Group from the Africa Israel Group for the purposes of the definition of a group of borrowers in the procedure. At the date of publication of this report no answer to this application has as yet been received from the Inspector of Banks.

21. **Material agreements**

21.1 **Financing agreement between Africa Financing and the company**

On September 13, 2004, Africa Investments and Africa Israel Financing (1985) Ltd. (hereinafter: "**Africa Financing**"), signed an agreement, according to which the company may, by mutual consent, from time to time, deposit monies with Africa Financing; and from time to time, at the company's request and with the agreement of Africa Financing, Africa Financing will deposit monies with the company. The deposits will be of the "ON CALL" type, for a period not exceeding one year from the date of deposit, and will bear a variable annual interest at the rate of the prime interest in use from time at Bank Leumi, with a deduction of 1.25% per annum. Calculation of the interest will be made once a week. Any deposit, or part of it, with the interest, will be returned to the company by Africa Financing within one bank business day from the company's first written request, as the matter might then stand. Equally, any deposit, or part of it, with the interest, will be returned to Africa Financing within one bank business day from Africa Financing's first written request, as the matter might then stand. Africa Financing has the right to settle any deposit deposited at Africa Financing by the company, with the inclusion of interest, at a prior notice of one bank business day, and the company may equally settle any deposit deposited by Africa Financing with the company, with the inclusion of interest, at a prior notice of one bank business day. At the end of one year from the date of depositing, a deposit will be automatically settled, even without any notification by Africa Financing or by the company. It was also stipulated that, in so far as one party to the agreement breaks in a material manner its obligations according to the framework of the agreement, the party which had kept the agreement will have the right to settle immediately all the deposits deposited by the failing party, and to offset them against any deposit deposited by the party which had kept the agreement, at the date of settlement. Africa Investments guarantees all the above obligations made by Africa Financing. To the exclusion of the guarantee by Africa Investments, the company was not given any additional collateral in connection with the deposits which will be deposited at Africa Financing. The Company has not undertaken to provide security for deposits made with it in future. This agreement is avoidable on three months notice, and it replaces the way in which the day to day financing activity was conducted that was standard practice between the parties to it up to September 2004. This agreement received the approval of the general meeting of the company on January 19, 2005.

21.2 Management agreement signed between the company and Africa Investments

In an agreement dated July 27, 2004, signed between the company on one side and Africa Investments on the other side (above and hereinafter in this subsection: "**the management agreement**"), Africa Investments undertook to provide the company (directly, by Africa Investments itself or through Africa Investment's subsidiaries) with management, consulting, and accompaniment services (hereinafter in this subsection: "**the management services**") for members of the company group. These services will be provided for a consideration of a quarterly payment of a sum that equals NIS 750,000, linked to the December 2003 index published on January 15, 2004 (hereinafter: "**the basic management fees**"), and the further sum that equals 6.5% of the pre-tax quarterly earnings in accordance with the company's quarterly consolidated financial statements (hereinafter: "**the additional management fees**"). In addition, the company made payments to Africa Investments up to the end of 2004 for the transferred employees, as specified below.

It was stipulated that the calculation of the additional management fees due to Africa Investments will be made according to the company's consolidated quarterly financial statements, and it was agreed that in the absence of profit or in the case of loss (Heaven forbid), management fees will consist of the basic management fees. Management fees will be paid to Africa Investments within 15 days of the date of publication of the company's quarterly financial statements, and in every quarter – for the quarter then ended.

The management agreement is valid for two years, commencing from January 1, 2004, and will be renewed automatically for one more year at the end of every calendar year, unless either party notified of a termination of the management agreement, at least 90 days prior to the end of the agreement period.

According to the management agreement, the management fees include a consideration for the provision of accompaniment services to the company's subsidiaries: Af-Sar Ltd., Givat Savyon Ltd., and Mekarkei Merkaz Ltd. (Center Real Estate), as well as to the Joint Transactions Owners of Rights in the Lev Talpiyot and Rehovot Park Projects (hereinafter in this subsection: "**The Joint Transactions in Talpiyot and Rehovot Park**"). Since management agreements exist between the above subsidiaries, the Joint Transactions in Talpiyot and Rehovot Park, and Africa Investments, Africa Investments assigned to the company all its rights of receiving management fees from the said subsidiaries and from Joint Transactions, commencing at the date the management agreement becomes valid.

Moreover, Africa Investments assigned to the company its rights, set out in the management agreement dated 16.9.1997 between itself and Merkaz Savyonim Management and Maintenance Ltd., which are connected with the management of the Savyonim mall.

The management services include only the services specified hereunder: the services of the chairman of the company's board of directors, and of the company's director general and services of directors (except for the outside directors), ongoing management advice on day to day and strategic business developments (business development) of the company group, financial management, accountancy and bookkeeping of the company group, internal audit by the Africa Investments internal auditor, computerized network management services of the company group, marketing and sales management of the company group including lettings and the grant of other use rights in respect of properties of the company group, engineering management (including advice and the handling of land registration, planning and construction and management of property portfolios) of the company group, handling the collection of rents in the company group, management of maintenance of the company group buildings, dealing with the affairs of the company group *vis a vis* authorities, coordination of legal advice in the company group, coordination of accountancy advice in the company group, the company group secretariat, administrative services and human resources services.

Expenses and payments to third parties involved in the management and activities of the company group's members are not included in the management fees and Africa Investment will not bear these charges. In case Africa Investments does, for any reason, bear such payments or expenses, the company will indemnify it for such payments or expenses.

The agreement stipulates that, if the company does employ a secretary general, outside the framework of the management agreement, then the quarterly basic management fees paid to Africa Investments will be reduced by the company, as specified in the management agreement.

And similarly, it was stipulated in the management agreement that the company will pay monthly to Africa Investments, in addition to the management fees, the full cost of the wages - including allocations for termination of employee-employer relationships - of the company's employees actually working in the marketing and maintenance of the above company group's properties (hereinafter in this sub-section - "**the transferred employees**"), whose duties and the costs of their salaries were specified in the management agreement. The foregoing arrangement in relation to the transferred employees came to an end in accordance with the terms of the management agreement, at the end of the 2004. It follows from this that commencing from January 2005, only the management fees, as defined above, are being transferred to Africa Investments.

According to the addendum to the management agreement dated August 29, 2004, starting on the 1st January 2005 (hereinafter in this sub-section - "**the date of transfer**"), the transferred employees were transferred to the company, to the effect that they are currently employed directly by the company.

Africa Investments undertakes to indemnify the company for any payment the company might make, directly or indirectly, in relation to the transferred employees, for the period before the date of transfer.

21.3 An agreement to limit Africa Investment's activities in the field of income-generating properties

21.3.1 In this section, the following terms will have the signification specified in the sentences immediately following the hyphen:

"The determining date" – the date the company's shares were registered for trade on the Tel Aviv Stock Exchange Ltd., according to the prospectus;

"The prospectus" – the prospectus offering company's securities, published on 21 September, 2004;

"Income-generating properties" – rental real estate properties for various uses, including, and without limiting the generality of the aforesaid, residence, parking, storage, archiving, office space, industry and commerce, including as part of office buildings, commercial centers, mall, industrial parks, etc.;

"Income-generating properties activities" – the acquisition, initiating, and construction and/or management of income-generating properties, including the acquisition of real estate rights, to be used for the initiation and construction of income-generating properties);

"Holding" and - "means of control" – as defined in the Securities Law, 1968;

"Control block" – the quantity of means of control of any kind, in a certain corporation, in a proportion of more than 50% of the total means of control of that kind, in the said corporation;

"Corporation controlled" by a certain person – a corporation in which that person holds a control block;

"The Companies law" – The Companies Law, 1999, and the regulations prescribed in it, as they might be from time to time;

"The areas of the limitation" – the entire world, with the exclusion of the United States, Russia, and the Commonwealth of Independent States.

21.3.2 On September 13, 2004, the company and Africa Investments signed an agreement to regulate the areas of their activities, and their legal relationships in this context (hereinafter: **"the delimitation of activities agreement"**).

21.3.3 Within the framework of the delimitations of activities agreement, Africa Investments undertook that, commencing with the determining date and until termination of 5 years from the determining date, it will not engage in any income-generating properties activity in the areas of the limitation, and will not hold a control block in any other corporation which is engaged in income-generating activities in the areas of

limitation, with the exception of such a corporation which is a "public company", as this term is defined in the Companies Law (hereinafter: "**the limitation**".)

In spite of the above said, it was agreed between the parties to the delimitations of activities agreement, that the limitation does not apply in any of the following situations:

- a. Where Africa Investments and/or a corporation controlled by Africa Investments, were engaged in income-generating properties activities at the time of the determining date, including –to remove all doubt – activities in income-generating properties which were acquired by Africa Investments and/or a corporation it controls, prior to the determining date, or properties that were managed by any of them prior to the determining date specified above.
- b. Where the income-generating properties are part of a real-estate project which is not, primarily, an income-generating properties project (such as commercial centers in residential neighborhoods, rental residential apartments in apartment buildings, commercial and office spaces in tourist and vacation resorts, hotels, spa and curing centers, etc.).
- c. Where the income-generating activity is carried out by the Company, or by a corporation controlled by it, causes a breach of a binding commitment given by the Company to any third party (such as, without derogating from the generality of the foregoing, stipulations made in the framework of debentures (series A) of the Company that have been issued in accordance with a Trust Deed dated February 5, 2004 and the debentures (Series B) issued in accordance with the prospectus, or financial conditions that are stipulated, if any, as part of the company's agreements with banking institutions).
- d. Where the income-generating activity is carried out in real estate areas that, at the determining date, were intended by Africa Investments or by a corporation under its control, as the case might be, for a use other than an income-generating property, or for a construction other than that of an income-generating property. The intention of Africa Investments or of a corporation under its control as aforesaid, will be determined on the basis of information regarding statutory planning - an approved plan, or a plan undergoing the procedures of the planning committee - where the aim of the plan (approved or under examination) is evidently to use the major part of real estate building rights to non-income-generating purposes.

In so far as a plan regarding real estate assets, whether approved or still in the process of examination, is designed to use the major part of building rights for the purposes of constructing income-generating properties, Africa Investment will attempt to base its intention to use the real estate for some purpose other than the construction of income-generating property, on information, including non-written information, received from the relevant real estate planning authorities (such as the engineer of the local authority or the planning personnel in the

relevant planning committee). Such information should indicate that there are reasonable grounds to expect a future approval of a plan which does not use the major part of its building rights, to purposes other than income-generating properties.

- e. Where the income-generating properties activity in question follows a tender (or a similar competitive process) to acquire and/or manage an income-generating property, but the company is not able to meet one or more of its stipulations, and cannot reasonably expect to do so in the future.
- f. Where there is a business opportunity in the field of income-generating properties and the company decided that it is not interested in this opportunity, as long as such a decision is approved by the company in accordance with the regulations of Chapter 5 of the Companies Law, regarding approval of "an extraordinary transaction", as defined in the Companies Law.

21.3.4 In order to remove all doubts, it is hereby made explicit that the regulations of the delimitations of activities agreement do not hinder the company from engaging in income-generating activities outside the areas of the limitation, and from engaging in any other activity in any other place, in Israel and abroad.

21.3.5 It was agreed between the parties that, if Africa Investments will no longer hold the control block in the company, for any reason whatsoever, each of the parties to the agreement may revoke the agreement within the agreement period (i.e. before the termination of 5 years from the determining date), by a written notice delivered at least 90 days beforehand, as specified in the delimitation of activities agreement.

21.3.6 It was also agreed between the parties that if the company will cease to be a subsidiary of Africa Investments, as this term is defined in the Restrictive Practices Law, 1988 (hereinafter: "**the Restrictions Law**"), and in accordance with the regulations of the Restrictions Law valid at the said time, this agreement will become a restrictive agreement, which contradicts the regulations of the Restrictions Law, then in this case the delimitation of activities agreement will be automatically revoked (unless a request to be considered within the scope allowed by these regulations, which the parties undertake to submit, is approved), as is specified in the delimitation of activities agreement.

22. Legal Proceedings

See Note 26 to the company's financial statements.

23. Goals and business strategy

It is clarified hereby, that the following information, contained in this section, includes prospective information, based only on the company's evaluations, and that these evaluations

might possibly not materialize, for reasons that are not within the company's knowledge at the date of this report.

The company seeks to broaden its existing activities abroad, while initiating entrance to additional countries. This with the purpose of, inter alia, spreading risks in parallel to locating and exploiting business opportunities, in order to maximize returns on its investments. At the same time, the company will continue its endeavors to develop in Israel projects in the B.O.T. and P.F.I., and other similar, methods. As a rule, the company's project development policy is characterized by the development of projects from the early stage of land acquisition to the full realization of the project and its marketing. Nevertheless, if the company can locate business opportunities to acquire income-generating properties in Israel and abroad, it will consider such an investment as well.

24. **Forecast – development in the coming year**

It is clarified hereby that the following information, contained in this section, includes prospective information, based only on the company's evaluations, and that these evaluations will possibly not materialize, for reasons which are not within the company's knowledge at the date of the report.

24.1 The main events that the company anticipates will occur during 2006 are set out in detail below:

- a. Commencement of the occupancy stage of the first buildings in the Airport City Project in Belgrade (in the first half of 2006)
- b. Commencement of the process of construction of the projects in Pradovice and in Bucharest (in the second half of 2006)
- c. Completion of the second stage of construction in the South Kirya Building in Tel Aviv (in the first half of 2006)
- d. Completion of the first stage of the Students Dormitories Project in Jerusalem (in the second half of 2006)

24.2 On March 23, 2006 the company's board of directors made a decision concerning progress in steps being taken prior to a possible flotation on the AIM exchanges in London, of one of its subsidiaries, in the framework of which the group's activity will be concentrated in Europe (except for Russia). The extent of the flotation and its date has not yet been decided and it is no means certain that the step outlined above will indeed be taken.

On March 23, 2005, the audit committee of the company and the board of directors approved a transaction by which the aforementioned subsidiary will enter into a contractual agreement with companies in the Africa Investments Group, the controlling shareholder in the company, and by virtue of which there will be transferred to the said subsidiary, a number of Czech and Bulgarian foreign companies that own the rights and/or have entered

into contractual agreements for the acquisition of rights in projects in the residential field in Prague and in Sofia, as well as balances of the owner's loans, and all for a consideration equivalent to the cost of the acquisition of such projects, the expenses accumulated in respect of them up to the date of closure of the transaction, and the owner's loan balances. As at December 31, 2005, the total amount of such cost, expenses and owner's loan balances as aforementioned, is approximately NIS 26,982 thousands. The agreement is subject to approval of the general meeting of the company's shareholders pursuant to Section 275 of the Companies Law, 5759-1999 being an agreement in which the controlling shareholder in the Company has a personal interest. As a consequence of this, such activity in the residential field is intended for inclusion as well in the framework of the subsidiary whose flotation is being considered by the company, as aforementioned.

CHAPTER 3 – MATTERS THAT CONCERN THE GROUP ACTIVITIES

25. **Financial information regarding geographical regions**

See Note 29 to the financial statements.

26. **Discussion of risk factors**

The company's main line of activity is income-generating real estate properties in Israel and abroad and therefore such activity exposes it to changes in the economy in Israel and in the various countries in which she is active, in general, and to the condition of the income-generating real estate market in particular. Such risks are:

26.1 **Macro risks** –

Growth rates and the extent of economic activity in Israel and in the countries in which the company operates have a significant effect on the dimensions of the demand for rental spaces, and on the dimensions of the activity in the company owned malls.

Changes in the interest rates in Israel and abroad and rate of the index rise in Israel affect the financing costs of the company.

26.2 **Sector risks** –

As a result of the condition of the Israeli economy during the last years, there are significant surpluses in the supply of the rental spaces market. The scope of these started to decrease in the course of 2005.

About 20 %- 23% of the company's income in the last years comes from clients from the hi-tech and biotechnology sector, and who rent space in the industrial parks. As a result, the company is exposed to changes in the activity in these fields.

About 38% of the company's income in 2005 came from renting commercial spaces in Ramat Aviv Mall and in Savyonim Mall, with the result that the company is exposed in some degree, to the activities of competing malls – of malls which are already operational, and of malls expected to open soon.

26.3 **Specific company group risks** -

See section 20 above, on the limitations on a group of borrowers, which apply to the company.

	Risk factor's degree of effect on the group as a whole		
	Strong effect	Medium effect	Small effect
<u>Macro-economic risk factors</u>			
The economic situation in Israel	X		
The economic situation outside Israel where the group operates		X	
Interest rates in Israel and abroad, where the group operated			X
The rate of change in the Consumers Price Index in Israel			X
<u>Sector risk factors</u>			
Over-supply of rental spaces		X	
Exposure to changes in the Hi-Tech Sector			X
Exposure to slowdown and competition in the malls sector			X
<u>Risk factors specific to the group</u>			
Single borrower limitations			X