

AFRICA ISRAEL PROPERTIES

BOARD OF DIRECTORS REPORT

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March 23, 2006

Adar 23, 5765

BOARD OF DIRECTORS REPORT FOR THE PERIOD JANUARY – DECEMBER 2005

1. General

The Company's net consolidated income together with those of its subsidiaries (hereinafter - "the Company" or "Africa Properties") in 2005 reached approximately NIS 53.3 million as opposed to NIS 140.6 million in 2004 (which includes a net capital gain of NIS 99.2 million from the sale of 50 % of the Palace Flora Shopping Center.

The Company's net income in the fourth quarter of 2005 amounted to approximately NIS 12.7 million as opposed to NIS 108.4 million in the corresponding quarter last year (including the aforementioned capital gain).

The following are data selected from the financial statements (in NIS millions):

	For year ended on		For the 3 months ended on	
	31.12.05	31.12.04	31.12.05	31.12.04
Revenues from leasing and operation of properties	234.2	232.0	61.2	60.6
Operating profit	155.1	152.4	40.6	39.5
Financing expenses, net	58.1	40.7	9.7	2.3
Other revenues	<u>22.9</u>	<u>125.0</u>	<u>1.0</u>	<u>124.4</u>
Net profit	<u>53.3</u>	<u>140.6</u>	<u>12.7</u>	<u>108.4</u>

2. **The main data from the description of the Corporation's business**

The Company operates in the field of income producing real estate since its establishment in 1971. It owns buildings used for industry, commerce and offices in Israel and abroad. In addition, it has building properties, land and building rights not yet utilized.

- 2.1 **Offices in Israel** – the Group of Companies' main offices in Israel are: the Africa Israel Tower in Tel Aviv; the Kirya Tower in Tel Aviv; a building office over the Ramat Aviv Shopping Mall; the Concorde Towers in Bnei Barak; various offices above the Savyonim Shopping Mall in Yahud.
- 2.2 **High tech industrial parks in Israel** – the Company Group has hi- tech industrial parks including the Kiryat Weitzman – Ness Ziona Science Park; Kiryat Hamada BeMigdal Ha'emek; the Global Park in Lod; and the park in Rehovot.
- 2.3 **Commerce in Israel** – the Company Group has shopping malls and additional trading areas in Israel, the main one being: the Ramat Aviv Mall in Tel Aviv and the Savyonim Mall in Yahud.
- 2.4 **Offices, commercial and logistic areas abroad** – the Company Group has a number of properties abroad, the main one being the Palace Flora Mall in Prague, the Czech Republic. In addition, the Company Group has additional commercial and office areas in Holland, 50% of the rights on a plot in Bucharest - Romania on which it is planned to build, *inter alia*, a Shopping Mall (see Section 4.4.2). The Company has commenced operations in Manila in the Philippines where it has acquired shares in a company that owns the rights to a park which contains office buildings, and additional building rights (see Section 4.5.4)
- 2.5 **Others** – in addition to the operations of the Company Group as detailed above:
 - a. The Company, through a Canadian subsidiary, in which the Company (indirectly) holds approximately 50% of the share capital, owns an apartment building for leasing in Toronto Canada. After the date of the balance sheet the Company Group entered into a contractual agreement for the sale of the aforementioned building
 - b. The Company Group is building student housing on Mount Scopus, Jerusalem by the B.O.T method.

3. Financial condition

The following are the highlights from the balance sheet in NIS millions:

	<u>December 31, 2005</u>	<u>December 31, 2004</u>
Total balance sheet	2,854	2,788
Shareholders' equity and minority rights	1,064	1,046
Long-term liabilities (including capital note)	1,292	1,264(*)
Short-term credit from banks and others	407	319
Current and other liabilities	91	159
Fixed assets	2,069	2,026
Investments in investee companies	22	47
Long-term loans and receivables	44	48
Cash and cash equivalents	218	247
Other current assets	482	401(*)

* Reclassification

During the period of the report no material changes have occurred in the majority of the balance sheet items. The assets of the Company and its subsidiaries presented in the consolidated balance sheet on December 31, 2005 reached NIS 2,854 million compared to NIS 2,788 million on December 31, 2004.

4. The results of the business operations

4.1 In December 2002 the Company acquired the main income-generating real estate properties of the Africa Israel Group abroad. In December 2003 the main income producing real estate assets of the Group in Israel were transferred to it, and therefore it is not possible to compare the results of the Company's operations in 2004 and 2005 to those of previous periods.

4.2 The following are the main data from the statement of income and expenditure for the years ended on December 31 (in NIS millions):

	<u>2005</u>	<u>2004</u>
Revenues from leasing and operating properties	234.2	232.0
Expenses from operating and maintaining properties	(36.8)	(34.3)
Depreciation and amortization	<u>(42.3)</u>	<u>(45.3)</u>
Operating income	155.1	152.4
General and administrative expenses	<u>(15.5)</u>	<u>(21.3)</u>
Income before financing	139.6	131.1
Financing expenses, net	(58.1)	(40.7)
Other revenues	<u>22.9</u>	<u>125.0</u>
Income before taxes on income	104.4	215.4
Taxes on income	<u>(19.3)</u>	<u>(57.0)</u>
Income after tax	85.1	158.4
Company's share in losses of affiliated companies	(14.2)	(7.0)
Minority share in income of consolidated companies	<u>(16.3)</u>	<u>(10.8)</u>
Accumulated effect due to change in method of accounting	<u>(1.3)</u>	--
Net income	<u>53.3</u>	<u>140.6</u>

- **Revenues from leasing and operating properties**

The Company's revenues from letting and operation of properties amounted, in 2005, to approximately NIS 234.2 million as compared to approximately NIS 232 million in 2004.

The revenues in 2005 include the Company's share in the revenues of the Kirya Tower in Tel Aviv, and only one half of the revenues of Palace Flora Mall in Prague, half of which was sold at the end of 2004.

- **Expenses of operating and maintaining properties**

Expenses of operating and maintaining properties amounted, in 2005, to approximately NIS 36.8 million as compared to approximately NIS 34.3 million in 2004.

- **Management and general expenses**

Management and general expenses amounted, in 2005, to approximately NIS 15.5 million as compared to approximately NIS 21.3 million in 2004.

- **Financing expenses**

The financing expenses amounted, in 2005, to approximately NIS 58.1 million as compared to approximately NIS 40.7 million in 2004.

The increase in expenditure stems principally from the rise in the CPI at a rate of 2.38% for 2005 as compared to 1.21% in 2004.

- **Taxes on Income**

In 2005 the tax expenditure amounted to approximately NIS 19.3 as compared to approximately NIS 57 million in the corresponding period in the previous year.

The decrease in the tax expenditure stems from calculation of the deferred tax balances in accordance with the new tax rates (see Note 25 to the financial statements), the total effect of the change having amounted to approximately NIS 6.5 million. Moreover, the tax expenditure in 2004 included tax in respect of the sale of 50% of the Palace Flora Mall.

In the period of the Report, the Company applied Accounting Standard No.19 for the first time in relation to taxes on income, the accumulated effect of which, for the beginning of the year due to the change in the system of accounting, amounted to an expense of approximately NIS 1.3 million.

- **The Company's Share in Losses of Affiliated Companies, Net**

This Item includes an expense of NIS 5.1 million in respect of the Company's share in the differential due to a fall in the value of fixed assets that are held by means of a joint transaction which is shown according to the balance sheet value method. The use value of the property is calculated by capitalization of the cash flows that are expected to arise from the property at a capitalization rate of 7.5%.

4.3 **The Company's statement of income and expenditure for 2005 on a quarterly basis in reported amounts (in NIS thousands):**

	1-3/05	4-6/05	7-9/05	10-12/05	For the year ended 31.12.05
	(unaudited)	(unaudited)	(unaudited)	(unaudited)	(audited)
Revenues					
From leasing and operating properties	56,748	57,249	58,942	61,224	234,163
Expenses					
From operations and maintenance of properties	9,406	8,579	9,105	9,671	36,761
Depreciation and amortization	10,644	10,388	10,292	10,970	42,294
General and administrative	4,311	2,925	3,478	4,833	15,547
Net financing	14,396	14,246	19,733	9,692	58,067
	38,757	36,138	42,608	35,166	152,669
Income from regular operations	17,991	21,111	16,334	26,058	81,494
Other revenues, net	14,471	1,131	6,315	1,018	22,935
Income before taxes on income	32,462	22,242	22,649	27,076	104,429
Taxes on income (tax benefit)	6,281	5,661	(2,926)	10,305	19,321
Income after taxes on income	26,181	16,581	25,575	16,771	85,108
Company's share of losses in affiliated companies, net	(1,444)	(2,801)	(8,145)	(1,767)	(14,157)
Minority's share in income of subsidiaries, net	(8,288)	(1,878)	(3,847)	(2,299)	(16,312)
Income from ongoing activities	16,449	11,902	13,583	12,705	54,639
Cumulative effect	(1,314)	--	--	--	(1,314)
Net income for the period	15,135	11,902	13,583	12,705	53,325

4.4 **Events during the period of the report**

- 4.4.1 In February 2005 completion occurred of a transaction in which a subsidiary company sold its assets and operations of one of its Canadian subsidiaries in which the subsidiary company holds (indirectly), 55% of the share capital.

Under the purchase agreement, two foreign companies acquired from the Canadian Company, the lands, buildings, lease contracts and the rights of the Canadian Company in goods and chattels, in relation to an apartments project consisting of approximately 103 housing units in Toronto - Canada, in consideration of approximately 20.7 Canadian Dollars. The subsidiary company recorded in its financial statements in respect of the transaction, for the reporting period, a profit (after tax) of approximately NIS 6.6 million.

- 4.4.2 In December 2005, a subsidiary company entered into a contractual agreement with a foreign company (hereinafter: "the seller"), controlled by an American Investment Fund which deals in real estate investments in Europe, regarding the acquisition (directly or indirectly through an associated corporation) of 50% of the seller's rights in a Cypriot Company (hereinafter: "the acquired company"), which owns land covering an area of approximately 120 dunams in the center of Bucharest, Romania (hereinafter: "the plot:). At the date of signature of the memorandum of understanding the seller holds approximately 98% of the rights in the acquired company.

The consideration for the rights of the acquired company was fixed at sum of approximately 9 million Euros. Real estate projects can be constructed on the plot under various zonings and for such purpose it was stipulated that the zoning of the plot would be determined subsequently by agreement between the parties. In the Company's estimation it will be possible to build various projects on the plot to an extent of at least 150,000 square meters. It was further agreed that the acquired company would be granted a right of first refusal for the acquisition of a further 40 dunams adjacent to the plot.

The transaction was completed at the beginning of 2006.

- 4.4.3 During the year transactions were completed in which affiliated companies of a subsidiary company (share of the subsidiary 49%) sold 3 properties in England for a consideration of approximately 45.4 million Pounds Sterling. The sale proceeds were used principally in repaying loans to banks totaling approximately 37.3 million Pounds Sterling and in repayment of loans from shareholders totaling approximately 4.0 million

Pounds Sterling, of which the Company's share was approximately 2.0 million Pounds Sterling.

As a result of sale of their assets the affiliated companies ceased their operations and entered into voluntary liquidation. The overall effect of the sale and liquidation (after tax) is a profit of approximately NIS 0.6 million in the Company's statements.

- 4.4.4 In December 2005, a transaction was completed for the sale of rights in the Vltava Park Project in Prague (Czech Republic) from a Czech company wholly owned by the subsidiary company, to a another Czech company in which the subsidiary company holds 50% (indirectly).
- 4.4.5 By September 30, 2005, 995,695 option warrants (Series 2) had been exercised for 99,569, 500 par value debentures (Series B) of the Company. The remaining option warrants (Series 2) which had not been exercised, expired on October 2, 2005. As at December 31, 2005, the balance of the debentures (Series b) included in the turnover is NIS 249,569,500 at par value.
- 4.4.6 In the period of the report the Company sold its rights in the Atarim car park as well as its rights in a plot in Migdal Ha'Emek for a consideration of approximately NIS 15.2 million. As a result of these transactions the Company recorded a net profit after tax amounting to approximately NIS 2 million.
- 4.4.7 On July 22, 2004, an option agreement was signed between Africa Investments and Bank Leumi in connection with the acquisition of shares in the Company. As part of this agreement the company granted Bank Leumi an option to purchase a quantity of the Company's shares which would constitute 5% of any class of the means of control (within the meaning of such term in the Securities Law 5728-1968) of the Company following 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 company which is wholly owned by Bank Leumi, all its rights and obligations under the option agreement. Further to the foregoing and on the same day, notice was received on behalf of Leumi and Co. of exercise of the option (which had been assigned as aforesaid by Bank Leumi). In accordance therewith 631,579 ordinary shares in the Company were allotted to Leumi and Co., in 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 closing prices of the Company's shares on any day's trading on the Stock Exchange over the 90 day period that preceded the exercise date), in other words, a total of approximately NIS 78.6 million.

4.4.8 In the framework of the Company's prospectus, Africa Investments undertook that on December 29, 2005, it would offer to purchase, during trading on the Stock Exchange, all the option warrants (Series 1) at a price of NIS 20 per option warrant (Series 1) linked to the Consumer Prices Index. In accordance with such undertaking Africa Investments purchased, on December 29, 2005, 273,259 option warrants (Series 1) at a price of NIS 20.52 per option warrant (Series 1). As at the date of this report Africa Investments holds 261,316 option warrants (Series 1).

4.5 **Events after the balance sheet date**

4.5.1 On March 8, 2006, the Company received notice from Bank Leumi Israel Ltd. (hereinafter: "the Bank") pursuant to which the Bank exercised its right to sell (Put Options) to the company and to obligate it to acquire, from the Bank, the Bank's shares in Af-Sar Ltd. (hereinafter: "Af-Sar"), namely 20% of the issued and paid up capital of Af-Sar.

Under the notice, the date of exercise of the said option will occur on April 9, 2006 and the exercise price has been determined at a total of NIS 51,400,000.

Upon completion of the exercise and payment of the consideration, as aforesaid, the Company will become the holder of the entire issued share capital in Af-Sar.

4.5.2 After the balance sheet date and up to this date, 130 option warrants (Series 1) have been converted for 130 of the company's ordinary shares of NIS 1 par value each.

4.5.3 After the balance sheet date and up to this date, 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 each.

4.5.4 After the date of the balance sheet a subsidiary company entered into a contract with CYBERZONE PROPERTIES INC., a foreign corporation registered in the Philippines (hereinafter: "the project company"), for the acquisition of 40% pf the project company's issued capital. The project company holds (directly and indirectly) leasing rights in a project under construction of a park complex of office buildings for companies in the field of information technology in metropolitan Manila, the Philippines (hereinafter: "the project"). The following is a brief outline of the main points of the transaction:

The subsidiary company entered into a contractual agreement with the project company for acquisition of shares by way of allotment (hereinafter: "the investment agreement") for a total consideration of approximately 10 Million US Dollars.

It was provided in the investment agreement that the investment would be made in three stages, detailed below as follows:

On the date of signature of the investment agreement shares of the project company would be allotted to the subsidiary to the effect that following the allotment the subsidiary would hold 25% of the issued capital of the project company, this being in consideration of approximately 5.1 million US Dollars.

In February 2007, further shares of the project company would be allotted to the subsidiary to the effect that following such allotment the subsidiary would hold 35% of the issued capital of the project company, this being in consideration of approximately 3 million US Dollars.

In February 2008, further shares of the project company would be allotted to the subsidiary to the effect that following such allotment the subsidiary would hold 40% of the issued capital of the project company, this being in consideration of approximately 2 million US Dollars.

As at the date of the balance sheet 5 buildings covering a total leased area of approximately 40,000 square meters, are built and let in their entirety on the project land area, the amount of the revenues from the rents in respect of the aforementioned buildings amounted, in the fourth quarter of 2005, to approximately 1.1 million US Dollars.

Within one complete month of the date of signature of the investment agreement, completion is expected of the erection of a further building in the project covering a total rented area of approximately 11,000 square meters and the building works for the construction of a seventh building in the project, covering a total rented area of approximately 11,000 square meters, are expected to start upon completion of the construction of the sixth building, as aforementioned.

Upon completion of construction of the project the number of the buildings is expected to amount to 19, this covering a total area of construction of approximately 210,000 square meters.

The rights to the land have been leased from a company that is owned by a party associated with the other shareholders in the project company to the effect that the project company will be entitled to the rents in respect of every building for a period of about 15 years.

In the estimation of the project company, the completion date for the project in its entirety is scheduled for 2012 and the total amount of the investment in the project at this stage is estimated at approximately 136 million US dollars.

- 4.5.5 After the date of the balance sheet a Canadian subsidiary, in which the subsidiary company holds (indirectly) approximately 55% of the share capital, entered into a contractual agreement for the sale of its assets and its operation (hereinafter: "the sale agreement").

Under the sale agreement, a foreign corporation will acquire from the Canadian company, its rights in land, buildings, lease agreements, its rights in other contracts and goods and chattels, in relation to a ten storey apartment building containing 232 housing units, in Toronto Canada, for a consideration of 43 million Canadian Dollars.

Upon completion of the transaction it is anticipated that the company will record a profit after tax of approximately NIS 18 million.

5. **Liquidity and sources of financing**

During the year of account the Company's sources of financing were mainly cash flows from day to day operating activities as well as conversion of options for convertible bonds and the exercise of the options by Bank Leumi, see Section 4.4.7 above.

5.1 **Total Company's assets were financed as follows:**

	<u>%</u>	<u>NIS millions</u>
Shareholders' equity and minority rights	37.3	1,064
Long-term liabilities (including capital note)	45.3	1,292
Current liabilities (including short-term credit from banks)	<u>17.4</u>	<u>498</u>
	<u>100.0</u>	<u>2,854</u>

About 37.3% of the Company's assets are financed by shareholders' equity and minority rights.

The working capital ratio as at December 31, 2005 was 1.4 (compared to 1.36 as at December 31, 2004).

5.2 **The following is a condensed statement of cash flows for the period ended on December 31, 2005 (in NIS millions):**

Sources

Net income	53.3	
Adjustments to income	6.8	
Net cash provided by operating activities	<u> </u>	60.1
Repayment of deposits		4.1
Issue of shares		78.6
Issue of bonds		107.2
Proceeds from realizing fixed assets		79.4
Consideration from sale of investment in investee and affiliated companies		140.4
Receipt of long-term loans from others, net		25.0
Decrease in cash balance		<u>28.6</u>
		<u>523.4</u>

Uses

Related companies, net		181.6
Repayment of short-term credit from banks		31.7
Repayment of long-term loans from others, net		0.3
Investment in fixed assets and other assets		168.0
Dividend paid to minority		12.0
Dividend paid		115.0
Loans made to investee companies		6.8
Investment in loans and receivables long term, net		<u>8.0</u>
		<u>523.4</u>

6. **Qualitative report regarding exposure to market risks and the methods of their management**

6.1 **General**

*"Market risk" – risk to the business results, to shareholders' equity, to cash flows or to the Company's value resulting from changes in interest, rates of exchange, inflation, price of raw materials, other prices, prices of securities in Israel and abroad and economic indices which significantly affect the Company's assets or liabilities, including the Company's liabilities to suppliers, trade receivables to the Company and other assets and loans.

The risks detailed below are managed on a current management level by the Company and the person responsible for their management is Mr. Pinchas Cohen – the Company's CEO.

Currency risks

The Company has credit in foreign currency and lease agreements denominated in foreign currency.

A revaluation of the loans that the Company took to finance its operations abroad and the proceeds of the lease agreements denominated in foreign currency are affected by fluctuations in rates of exchange.

The Company has an accounting exposure to changes in the rates of exchange on autonomous companies abroad. This exposure is for the difference between the value of the loans to these companies and their assets.

The Company has a surplus of liabilities linked to the euro resulting from financing its operations abroad (mainly in the Czech Republic) and a surplus of liabilities linked to the US dollar and to the Canadian dollar. Fluctuations in the rates of exchange affect the revaluation of these liabilities.

Interest risks

The Company makes use of short-term credit interest, short-term credit linked to the dollar, long-term credit linked to the index from banks, and long-term credit linked to the index from bond holders. In addition, the Company makes use of the financial instruments of borrowing bonds short.

For the financing of the operations abroad the Company takes credit in the currency of operations from banks abroad.

The Company considers from time to time the method of linkage of the loans according to its evaluations regarding developments in the rates of interest and the rates of inflation.

Changes in rates of "prime" interest in the economy are likely to cause a negative affect on the profitability of the Company.

Index risks

The Company has a surplus of liabilities linked to the index. In October 2001 the Israel Accounting Standards Board published Accounting Standard No. 12 which deals with the discontinuation of the adjustment of financial statements. On the new Standard coming into force at the beginning of 2004, the Company had an accounting exposure.

In the Company's opinion the exposure is not economic as in its evaluation the value of the Company's real estate assets over time increases at least by the rate of increase of the index.

The Corporation's policy regarding managing currency and interest risks

The Corporation has adopted a policy of taking loans or investing in deposits according to the currency of that relevant operation.

A decision regarding investments or taking credit in foreign currency are taken by the Company's Board of Directors or that of its subsidiaries.

The Company's management examines on a current basis the extent of its exposure and consults with local and international factors to reduce such exposure.

Supervision of the policy of managing market risks: The Company's Board of Directors at its periodic meetings receives current reports from the Company's management regarding market risk and the policy of managing these risks. No quantitative frameworks have been determined regarding exposure to market risks.

6.2 **Balance sheet as at December 31, 2005 according to base linkage (in NIS millions)**

Assets	Unlinked	Index linked	Euro linked	USD linked	CAD linked	Other	Non monetary items	Total
Fixed assets							2,069	2,069
Investments in investee companies		46					(24)	22
Long-term loans and receivables		10		34				44
Other assets and deferred expenses							19	19
Deferred taxes receivable							22	22
Customers	6					4		10
Debtors and debit balances	18	17	3		21	13		72
Related companies		376	1	1				378
Deposits								
Cash and cash equivalents	117	2	28		3	68		218
	141	451	32	35	24	85	2,086	2,854

6.2 **Balance sheet as at December 31, 2005 according to base linkage (in NIS millions) (contd.)**

Assets	Unlinked	Index linked	Euro linked	USD linked	CAD linked	Other	Non monetary items	Total
Shareholders' equity and liabilities								
Shareholders equity							968	968
Minority rights in investee companies							97	97
Capital note	40							40
<u>Long-term liabilities</u>								
Loans from banks	47	241	295					583
Loans from related companies	78							78
Bonds		434						434
Other long-term liabilities	26	25	60					111
Employer-employee related Liabilities.								--
Reserve for deferred taxes							45	45
<u>Short-term liabilities</u>								
Short-term credit from banks and others	133	136	9	53	76			407
Related companies		6	1	1				8
Other payables	32	28	9		9	5		83
	356	870	374	54	85	5	1,110	2,854
Net balance of balance sheet	(215)	(419)	(342)	(19)	(61)	80	976	--

6.3 **Balance sheet as at December 31, 2004 according to base linkage (in NIS millions)**

Assets	Unlinked	Index linked	Euro linked	USD linked	CAD linked	Other	Non monetary items	Total
Fixed assets							2,026	2,026
Investments in investee companies		38					9	47
Long-term loans and receivables	2	4		32	10			48
Other assets and deferred expenses							19	19
Deferred taxes receivable							16 (*)	16(*)
Costumers	5		1		1			7
Debtors and debit balances	26	2	128		1	1		158
Related companies		216						216
Deposits					4			4
Cash and cash equivalents	108	1	134		4			247
	141	261	263	32	20	1	2,070	2,788

6.3 **Balance sheet as at December 31, 2004 according to base linkage (in NIS millions) (contd.)**

Assets	Unlinked	Index linked	Euro linked	USD linked	CAD linked	Other	Non monetary items	Total
Shareholders equity and liabilities								
Shareholders equity							956	956
Minority rights in subsidiary companies							91	91
Capital	40							40
<u>Long-term liabilities</u>								
Loans from banks	27	274	295					596
Loans from related companies	75							75
Debentures		420						420
Other long-term liabilities	26	14	51					91
Employer-employee related Liabilities.								--
Reserve for deferred taxes							42 (*)	42 (*)
<u>Short-term liabilities</u>								
Short-term credit from banks and others	165	30	7	49	68			319
Related companies		28		3				31
Other payables	87	23	5	1	4	7		127
	420	789	358	53	72	7	1,089	2,788
Net balance of balance sheet	(279)	(528)	(95)	(21)	(52)	(6)	981	--

(*) Reclassification

6.4 Positions in the Company's financial derivatives as at December 31, 2005

The Company Group is involved in various transactions in derivative financial instruments in currencies. The following are details of the exposure to market risks and the methods of their management as at December 31, 2005 (in NIS thousands).

	Up to a year			
	Nominal value		Fair value	
	Long	Short	Asset	Liability
<u>Dollar/NIS</u>				
<u>Options</u>				
Sale of CALL dollar option (1)		9,206		36

- (1) For hedging purposes – not recognized for accounting purposes (PUT options sold are against loans in foreign currency that the Company borrowed. (The hedging is the amount of the premium)).

Maximum holdings of derivatives

The highest value during the year of account of total sale positions in derivatives is approximately NIS 32 million at a fair value of NIS 200 thousands.

7. Dividends

In April the Company paid a cash dividend to its shareholders amounting to NIS 75 Million

In December the Company paid a cash dividend to its shareholders amounting to NIS 40 Million

8. Disclosure regarding the internal auditor

According to a directive pursuant to Section 36A (b) of the Securities Law – 1968, the following is a disclosure regarding the internal auditor and his activities:

- Clause ‘a’ of the directive:** Name of auditor: Uriel Azran
Date of start of serving: 12/97
Qualifications: Certified Public Accountant
- Clause ‘b’ of the directive:** The auditor provides external services to the Corporation in the framework of a basket of services provided from the Parent Company.
- Clause ‘c’ of the directive:** The extent of employment: About one third of a full-time job.
The team of employees comprises two audit employees.
- Clause ‘d’ of the directive:** The audit program is based on a survey of risks carried out in the Corporation and by the current audit needs of the Company’s management.
The internal audit program includes significant Corporation matters based on the risks review carried out.
- Clause ‘e’ of the directive:** The internal audit program includes audit subjects in those Corporations which are significant holdings of the Corporation based on the risks survey carried out in them.
- Clause ‘f’ of the directive:** The internal auditor carries out an audit according to generally accepted professional standards in Israel and internationally.
- Clause ‘g’ of the directive:** The internal auditor reports to the Chairman of the Company’s Board of Directors.
- Clause ‘h’ of the directive:** The audit reports were submitted to the Chairman of the Board and to the Company’s CEO, the Chairman of the Audit Committee, and they have been discussed in the Audit Committee.
- Clause ‘i’ of the directive:** The level of the internal audit work is determined according to a rotation which enables the auditor to check significant matters in the Company about once every four years.

This extent, the character, the continuity of operations and the work program of the internal auditor, are reasonable in the opinion of the Company’s Audit Committee and are suitable to achieve the internal audit objectives in the Corporation. The Company declares that it has given the internal auditor in the Corporation free, continuous, and direct access to all information held by the Company.

9. Critical accounting estimates

In the preparation of the financial statements in accordance with generally accepted accounting principles management is required to use estimates and evaluations which affect the amounts reported of contingent assets and contingent liabilities which are disclosed in the financial statements and of data on revenues and expenses during the period of report. When preparing these estimates, the Company's management is required to make assumptions regarding the circumstances and the events connected with significant uncertainty.

Decline in value of assets

The Company has adopted Accounting Standard No. 15 "Decline in the Value of Assets". This Standard sets forth the accounting treatment and presentation required in the event in a decline in the value of the assets. The Standard applies to all assets appearing in the balance sheet excluding inventory, assets resulting from construction contracts, assets resulting from benefits to employees, and deferred tax assets and current assets (apart from investments in investee companies which are not subsidiaries).

According to this Standard, should there be any signs which would show a decline in the value of an asset, the Company must examine whether there was a decline in the value of the asset by comparing the book value of the asset to its recoverable value. The recoverable amount is the higher of the net selling price of the asset and the value of its use calculated by the present value of estimated future cash flows expected to be derived from the use of the assets and its realization at the end of its life.

Should the book value of an asset exceed its recoverable value, the loss on the decline in the value must be recognized as the difference between the assets book value and its recoverable value. The loss from the decline in value will be cancelled only if there were changes in the estimates used determining the recoverable value of an asset on the date of recognizing the loss from the decline in value.

The value of using the Company's assets (in consolidated) is generally calculated by discounting cash flows expected to result from the Company's assets (rate of discounting ranges between 7.5% - 9%) in the Dan region, in Haifa, Jerusalem and the capitals abroad, it is calculated by using a discounting rate of 7.5%.

In buildings where there are vacant areas, a reduction of 10% of the average rent in the building is taken into account.

In some of the projects where the Company has additional building rights on or attached to an existing project, and which the Company expects that it will make use of these rights in the future, some of the costs of the project are related to the second stage, i.e. to the stage of realizing the additional building rights.

In addition, where in an income producing property the value of all those areas that the Company has earmarked for sale is presented at an appraiser's value.

With regard to existing shopping malls – the rent resulting from them has a direct connection to the turnover of the shops in the shopping mall. The Company's evaluation of the recoverable amounts of a shopping mall are based on the Company's expectations to the malls' performance after a period of running-in of about two years. This is based on its experience in the field of shopping malls.

As a result of implementing the provisions of Accounting Standard No. 15 in the Company's financial statements (consolidated) for 2005 a loss from the decline in the value of assets of NIS 5,100 thousand was posted which is included in the item "the Company's share in losses of the affiliated companies", in the statement of income and expenditure.

In calculating the value of the Company's buildings (consolidated) future capital expenses were not taken into account, as in the opinion of the Company's management, current maintenance expenses, paid by tenants enable it to maintain the buildings in a conditions which does not required significant periodic capital investments.

Deferred taxes

Deferred taxes are calculated at tax rates expected to apply at the time of their realization. The tax benefit is included in the financial statements as according to the Company's business plan realization of the tax benefit is expected. Naturally, the actual business results can be different from the business plans, which could affect the realization of the tax benefit in the future.

Contingent liabilities

The Company has contingent liabilities in amounts where the maximum possible exposure for them is significant.

The Company periodically makes an evaluation of the potential liabilities relating to each claim and demand. Naturally, it is difficult to determine the results of claims and demands. The Company judges to the best of its ability and with the assistance of its legal advisors, in order to determine whether it is reasonable for the Company to bear costs in connection with settling claims and demands and whether it is possible to reasonably estimate them.

Taking into account the structural uncertainty which exists in legal claims, it is possible that all or part of them will end with a debit to the Company for different amounts.

With regard to details of contingent liabilities see Note 26 to the financial statements.

10. The Auditors Fee

- (a) The fees of the accountancy firms of Somekh Haikin and Zohar and Zohar and Co. (hereinafter: "**the Auditor**") which are paid by the Company Group in Israel in respect of auditing services, and audit related services, and for tax services, in relation to 2005, amounted to NIS 668 thousands (2004 - NIS 458 thousands). The audit fees of the firm carrying out the audit of the Company Group abroad (KPMG) in respect of auditing services, and for audit related services, and for tax services, in relation to 2005, amounted NIS 410 thousands (2004 - NIS 415 thousands).
- (b) The Auditor's fee for 2004, which the Company paid in connection with the listing of the Company for trading on the stock exchange, amounted to NIS 620 thousands.

The Auditor's fee (KPMG) paid by the Company Group abroad in respect of advice on various matters (principally tax advice) in relation to 2005, amounted to NIS 324 thousands (NIS 130 thousands in 2004).

11. The Company's Board of Directors and Management

During the period of report 7 meetings of the Company's Board of Directors and its committees took place and 6 written resolutions were passed.

On December 26, 2005 Mr. Leviev was appointed a Director of the Company and was also appointed as Chairman of the Board of Directors instead of Mr. Pinchas Cohen, who is continuing to serve as a Director of the Company.

On November 21, 2005, Shaul Gliksberg was appointed as a Director of the Company.

On January 1, 2006 Mr. Avraham Meron concluded his service as a Director of the Company.

On January 1, 2006 Mr. Beny Cohen concluded his service as a Director of the Company.

11.1 Details regarding Directors with special accounting and financial skill

Under the provisions of the Companies Law, 5759-1999 and the Regulations made pursuant thereto, the Board of Directors has decided that the required minimum number of Directors of the Company with special accounting and financial skill is two Directors.

This decision was made taking into account, *inter alia*, the size of the Company, its type of activities, the number of members of its Board of Directors and its complexity.

In the opinion of the Company, having regard to the overall relevant circumstances as detailed hereunder, the aforementioned stipulated minimum number will enable the Board of Directors to meet the legal obligations imposed upon it and in accordance with its documents of incorporation, and in particular in relation to its responsibility for examining the financial state of the Company and for preparation of the Company's financial statements, and this also in the event of the absence or illness of a Director with such expertise. Furthermore, the minimum number was determined taking into account the close supervision of the accountant seconded to the Company by the Company's Auditors, including their participation in meetings of the Board of Directors in which accountancy issues are discussed and their availability for questions by the Board of Directors.

The following are details of the names of the directors who have accounting and financial skills, with a brief statement of the facts regarding each of them from which it can be seen that they are each directors with accounting and financial skills:

Mr. Pinchas Cohen, the CEO of the Company and CEO of Africa Israel Investments Ltd., serves as a member of the Board of Directors of subsidiary companies in the Africa Israel Group. He holds a degree in Industrial Engineering and Management.

Mr. Shaul Gliksberg, a Certified Public Accountant, holds a degree in Accounting and Economics, serves as Senior Deputy CEO for Finance in Africa Israel Investments Ltd. and as a member of the Board of Directors of subsidiaries in the Africa Israel Group.

Mr. Avi Barzilai, a Certified Public Accountant, holds a degree in Accounting and Economics, serves as Senior Deputy CEO of the Company.

Mr. Mordechai Leibovich, Certified Public Accountant, holds a degree in Accounting and Economics, serves as CEO of Africa Israel Property Financing and Strategy Ltd (an investment house), and as a Director in subsidiaries of the Africa Israel Group.

All the Directors indicated above have previously signed financial statements and they are familiar with the functions of the auditor, the processes of preparation of financial statements and with the internal audit systems.

12. Survey of Members of the Public

In July 2005, the Securities Authority published a guideline pursuant to Section 36A (b) of the Securities Law, 5728-1968, concerning "disclosure as to the granting of consent to conducting a survey of members of the public" under which every reporting corporation is obliged to give details in the Board of Directors Report as to whether it has signified its consent to the delivery of the

required material for carrying out the sampling in relation to such a survey. On March 23, 2006 the Board of Directors resolved, pursuant thereto, that the Company would signify its agreement to delivery of the necessary material for the conducting the sampling in connection with the said survey by the Public Survey Institution of the Institute of Certified Public Accountants.

13. The Company's employees

The Board of Directors expresses its appreciation to the Company's management, to the management of the Company's subsidiaries and to all the employees for their dedicated work and contribution to the Company's advancement.

Lev Leviev
Chairman of the Board of Directors

Pinchas Cohen
Member of the Board of
Directors and CEO