

ZUR SHAMIR HOLDINGS LTD.

INTERIM CONSOLIDATED FINANCIAL STATEMENTS

AS AT MARCH 31, 2006

UNAUDITED

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The Board of Directors
Zur Shamir Holdings Ltd.

Dear Sirs,

Re: Review report of unaudited interim consolidated financial statements
for the three month period ended March 31, 2006

At your request, we have reviewed the interim consolidated balance sheet of Zur Shamir Holdings Ltd. as at March 31, 2006, and the related consolidated statement of profit and loss, statement of changes in shareholders' equity and consolidated statement of cash flows for the period of three months then ended. Our review was made in accordance with the procedures established by the Institute of Certified Public Accountants in Israel and included, among other things, reading the aforementioned financial statements, reading minutes of the meetings of the shareholders and of the Board of Directors and its committees and making inquiries of persons responsible for financial and accounting matters.

We have been furnished with reports of other accountants in respect of the review of the interim consolidated financial statements of certain subsidiaries, whose assets constitute approximately 6% of total consolidated assets as at March 31, 2006 and whose revenues constitute approximately 2% of total consolidated revenues for the three month period then ended.

Since the review performed was limited in scope and does not constitute an audit in accordance with generally accepted auditing standards, we do not express an opinion on the said interim consolidated financial statements.

Based on our review and the review reports of the other accountants, as mentioned above, we are not aware of any material modifications that should be made to the interim consolidated financial statements in order for them to be in conformity with generally accepted accounting principles and with the Securities Regulations (Periodical and Immediate Statements), 1970, taking into account that data regarding subsidiaries, which are insurance companies, are prepared according to generally accepted accounting and reporting principles prescribed by the Supervision of Financial Services (Insurance) Law, 1981.

Tel-Aviv,
May 30, 2006

KOST FORER GABBAY & KASIERER
A Member of Ernst & Young Global

CONSOLIDATED BALANCE SHEETS

	March 31,		December 31,	Convenience translation into U.S.\$ in thousands
	2006	2005	2005	
	Unaudited		Audited	
	Reported NIS in thousands			
CURRENT ASSETS				
Cash and cash equivalents	222,719	111,848	107,333	47,742
Short term investments	24,564	20,996	25,123	5,266
Customers	36,855	34,685	45,089	7,900
Insurance companies	56,395	46,352	49,619	12,089
Outstanding premiums	176,449	184,244	177,232	37,824
Debtors and receivables	53,909	45,458	49,103	11,556
	<u>570,891</u>	<u>443,583</u>	<u>453,499</u>	<u>122,377</u>
INVESTMENTS AND LONG TERM LOANS				
Investments of insurance companies	1,539,737	1,188,575	1,512,998	330,062
Reinsurers' share in insurance reserves and outstanding claims	111,719	101,639	116,564	23,948
Investment in affiliates and others	943	943	943	202
Long term investments	-	5,253	5,653	-
Loans	28,192	26,569	27,061	6,043
	<u>1,680,591</u>	<u>1,322,979</u>	<u>1,663,219</u>	<u>360,255</u>
FIXED ASSETS				
Cost	1,924,835	1,487,643	1,877,019	412,612
Less accumulated depreciation	272,199	243,765	273,792	58,349
	<u>1,652,636</u>	<u>1,243,878</u>	<u>1,603,227</u>	<u>354,263</u>
DEFERRED ACQUISITION COSTS AND OTHER ASSETS, NET				
Other assets and deferred expenses	164,739	37,528	130,053	35,314
Deferred acquisition costs in insurance companies	115,249	103,710	110,594	24,705
Deferred taxes	48,589	51,773	48,785	10,416
	<u>328,577</u>	<u>193,011</u>	<u>289,432</u>	<u>70,435</u>
	<u><u>4,232,695</u></u>	<u><u>3,203,451</u></u>	<u><u>4,009,377</u></u>	<u><u>907,330</u></u>

The accompanying notes are an integral part of the consolidated financial statements.

CONSOLIDATED BALANCE SHEETS

	<u>March 31,</u>		<u>December 31,</u>	<u>Convenience translation into U.S.\$ in thousands</u>
	<u>2006</u>	<u>2005</u>	<u>2005</u>	
	<u>Unaudited</u>		<u>Audited</u>	
	<u>Reported NIS in thousands</u>			
CURRENT LIABILITIES				
Credit from banking institutions	158,969	196,618	278,036	34,077
Suppliers and service providers	38,055	44,745	46,019	8,157
Insurance companies	16,359	16,739	16,752	3,507
Creditors and payables	172,595	132,656	130,768	36,998
Current maturities of capital notes convertible into Company shares	-	2,524	510	-
Current maturities of debentures convertible into subsidiary shares	6	6	6	1
	<u>385,984</u>	<u>393,288</u>	<u>472,091</u>	<u>82,740</u>
LONG TERM LIABILITIES				
Capital notes convertible into Company shares	-	639	-	-
Debentures convertible into subsidiary shares	11	16	11	2
Company debentures	351,010	100,000	303,557	75,243
Subsidiary debentures	528,923	150,000	456,930	113,381
Loans from banking institutions and others	1,081,103	789,362	925,796	231,748
Liability to cover an affiliate's losses	8,359	1,143	6,491	1,792
Deferred taxes	41,936	31,263	42,612	8,990
Liabilities for severance pay, net	871	1,519	780	187
	<u>2,012,213</u>	<u>1,073,942</u>	<u>1,736,177</u>	<u>431,343</u>
INSURANCE RESERVES AND OUTSTANDING CLAIMS	<u>1,425,562</u>	<u>1,279,921</u>	<u>1,402,415</u>	<u>305,587</u>
MINORITY INTEREST	<u>249,015</u>	<u>279,964</u>	<u>240,142</u>	<u>53,379</u>
RECEIPTS ON ACCOUNT OF OPTIONS REALIZABLE INTO SUBSIDIARY SHARES	<u>5,410</u>	<u>5,010</u>	<u>5,410</u>	<u>1,160</u>
SHAREHOLDERS' EQUITY				
Share capital	211,889	211,413	211,877	45,421
Capital reserves	63,817	52,159	58,575 *)	13,680
Retained loss	(60,021)	(31,072)	(56,136) *)	(12,866)
	<u>215,685</u>	<u>232,500</u>	<u>214,316</u>	<u>46,235</u>
Treasury shares	(61,174)	(61,174)	(61,174)	(13,114)
	<u>154,511</u>	<u>171,326</u>	<u>153,142</u>	<u>33,121</u>
	<u>4,232,695</u>	<u>3,203,451</u>	<u>4,009,377</u>	<u>907,330</u>

*) Restatement, see Note 2b(4).

The accompanying notes are an integral part of the consolidated financial statements.

<u>May 30, 2006</u>			
Date of approval of the financial statements	S. Schneidman Chairman of the Board of Directors	M. (Moki) Schneidman Member of the Board of Directors and Managing Director	R. Nakar Finance Director

CONSOLIDATED STATEMENTS OF PROFIT AND LOSS

	Three months ended		Year ended	Convenience translation into U.S.\$ in thousands
	March 31,		December 31,	
	2006	2005 *)	2005	
	Unaudited		Audited	
	Reported NIS in thousands			
	[except for earnings (loss)per share data]			
Income				
From insurance business	219,841	209,673	886,908	47,126
From lease of assets	32,807	27,210	114,642	7,033
From asset management and stock exchange services	2,457	3,190	11,462	527
From sale of software	-	2,928	2,928	-
Other income, net	5,881	7,049	11,329	1,260
	<u>260,986</u>	<u>250,050</u>	<u>1,027,269</u>	<u>55,946</u>
Costs and expenses				
Insurance business	205,280	192,148	802,034 *)	44,004
Maintenance of assets:				
Depreciation	7,057	5,741	24,591	1,513
Others	5,665	4,834	24,011	1,214
From asset management and stock exchange services	6,290	4,219	21,527	1,348
Cost of software sales	-	6,250	6,250	-
Administrative and general expenses	1,857	1,194	8,679	398
Financing, net	24,617	13,211	66,584	5,278
	<u>250,766</u>	<u>227,597</u>	<u>953,676</u>	<u>53,755</u>
Income before income taxes	10,220	22,453	73,593	2,191
Income taxes	6,434	13,137	50,563	1,379
Income after income taxes	3,786	9,316	23,030	812
Company's share in losses of affiliates	(1,868)	-	(5,347)	(401)
Minority share in profits of subsidiaries	(5,803)	(5,437)	(26,868) *)	(1,244)
Income (loss) for the period, before cumulative effect as at beginning of the period	(3,885)	3,879	(9,185)	(833)
Cumulative effect as at beginning of the period of change in accounting policies, net	-	(2,121)	(2,121)	-
Net income (loss) for the period	<u>(3,885)</u>	<u>1,758</u>	<u>(11,306)</u>	<u>(833)</u>
Earnings per share:				
Net earnings (loss) per ordinary share (NIS):				
Basic				
Before cumulative effect, net	(0.08)	0.06 *)	(0.11)*)	(0.02)
Cumulative effect, net	-	(0.04)*)	(0.04)*)	-
Net earnings (loss) for the period	<u>(0.08)</u>	<u>0.02 *)</u>	<u>(0.15)*)</u>	<u>(0.02)</u>

*) Restatement, see Note 2b (4).

The accompanying notes are an integral part of the consolidated financial statements.

STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

	Share capital	Share premium	Capital reserves	Adjustments due to translation of subsidiaries' financial statements	Retained loss	Treasury shares	Dividend declared after balance sheet date	Total
	Reported NIS in thousands							
Balance as at January 1, 2005 (Audited)	210,657	25,512	2,213	26,736	(32,830)	(61,174)	-	171,114
Conversion of capital notes	1,221	2,153	-	-	-	-	-	3,374
Adjustments due to translation of financial statements of foreign subsidiaries	-	-	-	1,355	-	-	-	1,355
Tax benefits in respect of capital instruments for subsidiary employees	-	-	375	-	-	-	-	375
Share based payment costs	-	-	230 *)	-	-	-	-	230
Dividend paid	-	-	-	-	(12,000)	-	-	(12,000)
Loss for the year	-	-	-	-	(11,306) *)	-	-	(11,306)
Balance as at December 31, 2005 (Audited)	211,878	27,665	2,818	28,091	(56,136)	(61,174)	-	153,142
Adjustments due to translation of financial statements of foreign subsidiaries	-	-	-	3,885	-	-	-	3,885
Tax benefits in respect of capital instruments for subsidiary employees	-	-	27	-	-	-	-	27
Share based payment costs	-	-	1,311	-	-	-	-	1,311
Conversion of capital notes	11	20	-	-	-	-	-	31
Loss for the period	-	-	-	-	(3,885)	-	-	(3,885)
Balance as at March 31, 2006 (Unaudited)	211,889	27,685	4,156	31,976	(60,021)	(61,174)	-	154,511
	Share capital	Share premium	Capital reserves	Adjustments due to translation subsidiaries financial statements	Retained loss	Treasury shares	Dividend declared after balance sheet date	Total
	Reported NIS in thousands							
Balance as at January 1, 2005 (Audited)	210,657	25,512	2,213	26,736	(32,830)	(61,174)	-	171,114
Adjustments due to translation of financial statements of foreign subsidiaries	-	-	-	(3,511)	-	-	-	(3,511)
Conversion of capital notes	756	1,209	-	-	-	-	-	1,965
Dividend declared after the balance sheet date	-	-	-	-	(12,000)	-	12,000	-
Net income for the period	-	-	-	-	1,758	-	-	1,758
Balance as at March 31, 2005 (Unaudited)	211,413	26,721	2,213	23,225	(43,072)	(61,174)	12,000	171,326

*) Restatement, see Note 2b (4).

The accompanying notes are an integral part of the consolidated financial statements.

STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

	<u>Share capital</u>	<u>Share premium</u>	<u>Capital reserves</u>	<u>Adjustments due to translation of subsidiaries' financial statements</u>	<u>Retained loss</u>	<u>Treasury shares</u>	<u>Dividend declared after balance sheet date</u>	<u>Total</u>
<u>Convenience translation into U.S. \$ in thousands</u>								
Balance as at December 31, 2005 (Audited)	45,419	5,930	604	6,022	(12,033)	(13,114)	-	32,828
Adjustments due to translation of financial statements of foreign subsidiaries	-	-	-	833	-	-	-	833
Tax benefits in respect of capital instruments for subsidiary employees	-	-	6	-	-	-	-	6
Share based payment costs	-	-	281	-	-	-	-	281
Conversion of capital notes	2	4	-	-	-	-	-	6
Loss for period	-	-	-	-	(833)	-	-	(833)
Balance as at March 31, 2006 (Unaudited)	<u>45,421</u>	<u>5,934</u>	<u>891</u>	<u>6,855</u>	<u>(12,866)</u>	<u>(13,114)</u>	<u>-</u>	<u>33,121</u>

The accompanying notes are an integral part of the consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Three months ended		Year ended	Convenience translation into U.S.\$ in thousands
	March 31,		December 31,	
	2006	2005	2005	
	Unaudited		Audited	
Reported NIS in thousands				
CASH FLOWS FROM CURRENT ACTIVITIES				
Net income (loss) for the period	(3,885)	1,758	(11,306) *)	(833)
Income (loss) from insurance business	1,933	(5,586)	(20,896) *)	415
	(1,952)	(3,828)	(32,202)	(418)
Adjustments required to present cash flows from current activities (A)	17,854	5,467	33,113	3,827
Net cash provided by current activities not including insurance business	15,902	1,639	911	3,409
Net cash provided by current activities in life assurance business (b)	4,907	1,852	16,934	1,052
Net cash provided by (used in) current activities in general insurance business(c)	(3,255)	(10,529)	5,595	(698)
Net cash used in other current activities in insurance business (d)	(13,067)	(10,672)	(30,153)	(2,801)
	4,487	(17,710)	(6,713)	962
CASH FLOWS FROM INVESTMENT ACTIVITIES				
Acquisition of a subsidiary's shares and bonds from minority shareholders	(2,256)	-	(11,031)	(484)
Exit from consolidation of a previously consolidated subsidiary (e)	1,698	(430)	(430)	364
Proceeds from realization of affiliates	-	2,228	2,228	-
Acquisition of fixed assets	(43,562)	(23,683)	(380,129)	(9,338)
Proceeds from sale of fixed assets	19,217	50,763	53,009	4,119
Realization of securities, net	5,866	282	(2,707)	1,258
Settlement of long term loans	5	-	16	1
Other assets and deferred expenses	(41,444)	(27)	-	(8,884)
Granting of long term loans	-	-	(135)	-
Net cash provided by (used in) investment activities not including insurance business	(60,476)	29,133	(339,179)	(12,964)
Net cash provided by (used in) investment activities in insurance business (f)	3,121	(31,619)	(320,280)	669
	(57,355)	(2,486)	(659,459)	(12,295)
CASH FLOWS FROM FINANCING ACTIVITIES				
Surrender of convertible capital notes	-	-	(1,366)	-
Settlement of bonds convertible into subsidiary shares	-	-	(6)	-
Issue of bonds of a subsidiary	87,579	-	42,500	18,774
Issue of bonds	54,615	-	199,232	11,707
Issue of shares to a minority in subsidiaries (net of issue expenses)	8,155	9,217	26,163	1,748
Settlement of long term loans from banking institutions	(17,337)	(62,230)	(137,715)	(3,716)
Receipt of long term loans from banking institutions	128,001	10,482	269,242	27,438
Decrease in short term credit from banking institutions, net	(96,332)	(9,178)	(9,860)	(20,650)
Payment of a dividend to a minority in a subsidiary	-	-	(4,503)	-
Dividend paid	-	-	(12,000)	-
Net cash provided by (used in) financing activities	164,681	(51,709)	371,687	35,301
Net cash provided by financing activities in insurance business (g)	158	-	217,432	34
	164,839	(51,709)	589,119	35,335
Translation differences in relation to cash balances in foreign autonomic subsidiaries	3,415	(3,035)	(2,402)	732
Increase (decrease) in cash and cash equivalents	115,386	(74,940)	(79,455)	24,734
Balance of cash and cash equivalents at the beginning of the period	107,333	186,788	186,788	23,008
Balance of cash and cash equivalents at the end of the period	222,719	111,848	107,333	47,742

*) Restatement, see Note 2b.

The accompanying notes are an integral part of the consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Three months ended		Year ended	Convenience translation into U.S.\$ in thousands
	March 31,		December 31,	
	2006	2005	2005	
	Unaudited		Audited	
	Reported NIS in thousands			
A. Adjustments required to present cash flows from current activities not including insurance business				
Income and expenses not involving cash flows:				
Company's share in losses of affiliate	1,868	-	5,347	400
Minority's share in income of subsidiaries	2,314	2,851	5,035	496
Depreciation and amortization	10,332	6,269	31,640	2,215
Capital gain, net	(3,535)	(4,169)	(6,403)	(758)
Capital gain from issue to a third party	(530)	(1,920)	(6,394)	(114)
Deferred taxes, net	(348)	827	2,023	(75)
Capital gain from realization of investment in a subsidiary	(781)	-	-	(167)
Liabilities for severance pay, net	(14)	(229)	(863)	(3)
Decrease (increase) in value of securities, net	346	(176)	(1,714)	74
Interest and erosion of loans and long term liabilities, net	(1,980)	2,596	30,887	(424)
	<u>7,672</u>	<u>6,049</u>	<u>59,558</u>	<u>1,644</u>
Changes in assets and liabilities:				
Decrease (increase) in customers	8,879	(592)	(11,520)	1,904
Increase in debtors and receivables	(14,395)	(5,867)	(13,037)	(3,086)
Decrease in suppliers and service providers	(9,483)	(3,280)	(2,347)	(2,033)
Increase in creditors and payables	25,181	9,157	459	5,398
	<u>10,182</u>	<u>(582)</u>	<u>(26,445)</u>	<u>2,183</u>
	<u>17,854</u>	<u>5,467</u>	<u>33,113</u>	<u>3,827</u>

The accompanying notes are an integral part of the consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Three months ended		Year ended	Convenience translation into U.S.\$ in thousands
	March 31,		December 31,	
	2006	2005	2005	
	Unaudited		Audited	
	Reported NIS in thousands			
B. Cash flows from current activities in life assurance business				
Income from life assurance business	3,637	3,106	9,531	780
Items not involving cash flows:				
Increase in insurance reserves net of reinsurance	11,436	9,167	40,461	2,451
Increase (decrease) in outstanding claims net of reinsurance	(51)	(28)	166	(11)
Depreciation	245	204	937	53
Investments, net:				
Securities	(11,058)	(7,760)	(36,952)	(2,370)
Bank deposits	95	108	(397)	20
Loans	(24)	(157)	(1,010)	(5)
Changes in other balance sheet items, net				
Insurance companies	1,009	(2,339)	2,997	216
Outstanding premiums	(220)	(239)	(110)	(47)
Debtors and receivables	79	(39)	(89)	17
Creditors and payables	(241)	(171)	1,400	(52)
Net cash provided by current activities in life assurance business	<u>4,907</u>	<u>1,852</u>	<u>16,934</u>	<u>1,052</u>
C. Cash flows from current activities in general insurance business				
Income from general insurance business	19,719	13,282	75,595	4,227
Items not involving cash flows:				
Increase in insurance reserves net of reinsurance	13,669	24,634	17,365	2,930
Increase (decrease) in outstanding claims net of reinsurance	(1)	18,792	100,428	-
Increase in deferred acquisition costs	(1,957)	(3,882)	(5,356)	(420)
Depreciation	1,973	3,773	16,887	423
Investments, net				
Securities	(27,979)	(82,205)	(218,274)	(5,998)
Bank deposits	7,054	7,700	6,480	1,512
Changes in other balance sheet items, net:				
Insurance companies	(8,178)	4,573	(4,005)	(1,753)
Outstanding premiums	1,490	1,701	8,844	319
Debtors and receivables	(1,276)	(1,038)	689	(274)
Creditors and payables	(7,769)	2,141	6,942	(1,664)
Net cash provided by (used in) current general insurance business	<u>(3,255)</u>	<u>(10,529)</u>	<u>5,595</u>	<u>(698)</u>

The accompanying notes are an integral part of the consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Three months ended		Year ended	Convenience translation into U.S.\$ in thousands
	March 31,		December 31,	
	2006	2005	2005	
	Unaudited		Audited	
	Reported NIS in thousands			
D. Cash flows from other current activities in insurance business				
Net profit (loss) for the period from insurance business	(1,933)	5,586	20,896 *)	(414)
Profit from general insurance and life assurance business	(23,356)	(16,388)	(85,126)	(5,007)
	(25,289)	(10,802)	(64,230)	(5,421)
Items not involving cash flows:				
Deferred taxes	(920)	316	1,265	(197)
Minority's share in profits of subsidiaries	3,489	1,807	21,054 *)	748
Capital loss (gain)	31	(1,811)	(193)	7
Depreciation and amortization	2,636	1,915	8,833	565
Erosion of subordinated deeds	1,487	-	6,579	319
Share based payment	1,997	-	350 *)	428
Changes in other balance sheet items, net				
Increase in deferred acquisition costs in insurance	(2,204)	(2,280)	(7,359)	(473)
Decrease (increase) in debtors and receivables	7,616	(429)	2,193	1,632
Increase (decrease) in creditors and payables, net	(1,910)	612	1,355	(409)
Net cash used in other current activities in insurance business	(13,067)	(10,672)	(30,153)	(2,801)
E. Exit from consolidation of company consolidated in the past				
Capital gain from realization of investment in a subsidiary	781	-	-	167
Working capital (excluding cash and cash equivalents)	(1,599)	(4,547)	(4,547)	(343)
Related companies	-	1,143	1,143	-
Fixed assets, net	3,534	1,295	1,295	758
Long term liabilities	(1,018)	-	-	(218)
Capital reserve from acquisition of a related company	-	1,679	1,679	-
	1,698	(430)	(430)	364

*) Restatement – see Note 2b.

The accompanying notes are an integral part of the consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Three months ended		Year ended	Convenience translation into U.S.\$ in thousands
	March 31,		December 31	
	2006	2005	2005	
	Unaudited		Audited	
	Reported NIS in thousands			
F. Cash flows from investment activities in insurance companies				
Decrease (increase) in investments in insurance companies, net	7,647	(26,194)	(182,299)	1,639
Acquisition of minority shares in a subsidiary	-	-	(116,292)	-
Acquisition of fixed assets	(4,616)	(5,356)	(21,708)	(989)
Other assets	-	-	(1,122)	-
Proceeds from sale of fixed assets	90	31	1,141	19
Net cash used in investment activities	<u>3,121</u>	<u>(31,619)</u>	<u>(320,280)</u>	<u>669</u>
G. Cash flows from financing activities in insurance companies				
Issue of subordinated deeds net of issue expenses	-	-	240,278	-
Proceeds from realization of shares in insurance subsidiaries	158	-	1,823	34
Dividend paid to minority in insurance subsidiaries	-	-	(24,669)	-
	<u>158</u>	<u>-</u>	<u>217,432</u>	<u>34</u>
H. Significant activities not involving cash flows				
Capital issue against conversion of convertible capital notes	<u>31</u>	<u>1,965</u>	<u>3,374</u>	<u>7</u>
Acquisition of fixed assets against suppliers and service providers	<u>1,392</u>	<u>-</u>	<u>1,605</u>	<u>298</u>
Sale of building against debtors and receivables	<u>-</u>	<u>4,908</u>	<u>4,431</u>	<u>-</u>
Acquisition of other assets against creditors and payables	<u>16,142</u>	<u>-</u>	<u>-</u>	<u>3,460</u>

The accompanying notes are an integral part of the consolidated financial statements.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 1:- GENERAL

- a. These financial statements have been prepared in a condensed format as of March 31, 2006, and for the three month period then ended (hereunder - interim financial statements). These financial statements should be read in conjunction with the Company's audited annual financial statements and accompanying notes as at December 31, 2005 and for the year then ended.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES

- a. The interim financial statements have been prepared in accordance with generally accepted accounting principles for the preparation of financial statements for interim periods, as prescribed in Accounting Standard No. 14 of the Israel Accounting Standards Board and in accordance with Chapter D to the Securities Regulations (Periodic and Immediate Reports), 1970.

The significant accounting policies and methods of computation applied in the preparation of the interim financial statements are identical to those applied in the preparation of the latest annual financial statements, except as described in section b below.

- b. Initial adoption of new Accounting Standards
 1. Initial adoption of Accounting Standard No. 20 (Revised) regarding the accounting for goodwill and intangible assets upon acquisition of investee

On January 1, 2006, the Company adopted the provisions of Accounting Standard No. 20 (Revised), Accounting for Goodwill and Intangible Assets upon Acquisition of Investee" (hereunder - the Standard), of the Israel Accounting Standards Board. The Standard prescribes the accounting treatment of goodwill and intangible assets upon the acquisition of a subsidiary and an investee which is not a subsidiary, including a company under joint control. In accordance with the provisions, the Standard is being applied prospectively and comparative data have not been restated.

The principal changes promulgated by the Standard in contrast to the principles applied prior to January 1, 2006 are: allocating the excess of cost of an investment in an investee also to the investee's identifiable intangible assets; distinguishing between intangible assets with a finite useful life and intangible assets with an indefinite useful life; immediate recognition as a gain in the statement of income of the balance of negative goodwill arising upon acquisition and remaining after deduction from the cost of the investee's intangible assets and non-monetary assets; the discontinuance of the systematic amortization of goodwill and intangible assets with an indefinite useful life; assessment for impairment of goodwill in respect of a subsidiary or jointly controlled company and of intangible assets with an indefinite useful life on an annual basis, or more frequently, if there are indications of impairment; distinguishing between goodwill relating to the acquisition of a subsidiary and a jointly controlled company as opposed to that of an affiliate in respect of the assessment of impairment, such that impairment of goodwill for an affiliate is evaluated in the context of the assessment of impairment of the investment as a whole. Impairment is accounted for in accordance with Accounting Standard No. 15, "Impairment of Assets".

NOTES TO THE FINANCIAL STATEMENTS

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)b. Initial adoption of new Accounting Standards (Cont.)1. Initial adoption of Accounting Standard No. 20 (Revised) regarding the accounting for goodwill and intangible assets upon acquisition of investee (Cont.)

As a result of the initial adoption of the provisions of the Standard:

The Company discontinued the systematic amortization of goodwill which amounted to about NIS 1,418 thousand and about NIS 7,358 thousand for the three months ended March 31, 2006, and for the year ended December 31, 2005, respectively. The balance of goodwill as of January 1, 2006 is NIS 76,244 thousand.

2. Initial adoption of Accounting Standard No. 21 regarding earnings per share

Beginning January 1, 2006 (the effective date), the Company adopted the provisions of Accounting Standard No. 21, Earnings per Share (hereunder - the Standard) of the Israel Accounting Standards Board. The Standard prescribes the principles for the computation and presentation of earnings (loss) per share in the financial statements and supersedes Opinion No. 55 of the Institute of Certified Public Accountants in Israel.

According to the Standard, earnings per share are computed based on the number of ordinary shares (and not per NIS 1 par value of the shares as computed until the effective date). Basic earnings per share include only shares which are outstanding during the period whereas convertible securities (such as convertible debentures and options) are only included in the computation of diluted earnings per share, in contrast to the principles applied until the effective date according to which in cases where a convertible security is likely to be converted, it is included in the computation of basic earnings per share. In addition, convertible securities which are converted during the period, are included in diluted earnings per share up to the date of conversion and are included in basic earnings per share from that date. Pursuant to the Standard, options are included in diluted earnings when their exercise results in the issuance of shares for a consideration which is less than the market price of the shares. The amount of dilution is the market price of the shares minus the amount that would have been received as a result of the conversion of the options into shares. This is in contrast to the method of computation prescribed by Opinion No. 55, which also included adjustments to earnings.

The Company's share in profits of investees is computed according to the earnings per share of those investees multiplied by the number of shares held by the Company.

As a result of the initial adoption of the provisions of the Standard, the comparative figures of earnings per share relating to previous periods have been restated. These comparative figures, prior to restatement, were NIS 0.03 and NIS (0.19) for basic earnings per share (per NIS 1 par value) for the three months ended as at March 31, 2005, and for the year ended December 31, 2005, respectively.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)b. Initial adoption of new Accounting Standards (Cont.)3. Initial adoption of Accounting Standard No. 22 regarding financial instruments: disclosure and presentation

Beginning January 1, 2006 (the effective date), the Company adopted the provisions of Accounting Standard No. 22, Financial Instruments: Disclosure and Presentation (hereunder - the Standard) of the Israel Accounting Standards Board. The Standard prescribes principles for the presentation and disclosure of financial instruments and supersedes Opinions No. 48 and 53 of the Institute of Certified Public Accountants in Israel. In accordance with the Standard, the Standard is being applied prospectively and comparative data have not been restated or reclassified.

The principal changes promulgated by the Standard in contrast to the principles applied to today are: transaction costs in respect of a financial liability are deducted from the liability and are taken into account in the computation of the effective interest rate; upon the issuance of several types of financial instruments in a single unit (shares, debentures and option warrants), the components of the unit, including related transaction costs, are classified separately upon initial recognition into the various financial instruments based on their fair value; compound financial instruments that include both a liability and an equity component (such as convertible debentures) are bifurcated between the equity component (receipts from conversion option) and the liability component and each component is classified separately (net of transaction costs attributed to the different components).

The Standard supersedes the provisions of Opinions No. 48 and 53 of the Institute of Certified Public Accountants in Israel, according to which in certain circumstances, an investor was required to record a provision for a loss resulting from a decrease in its holdings in an investee, due to the probable conversion of convertible instruments issued by the investee (hereunder - loss provision).

Transaction costs in respect of financial liabilities are deducted from the liabilities and taken into account in the computation of the effective interest rate. The balance of issuance expenses, in the amount of NIS 20,489 thousand as of December 31, 2005, in respect of convertible debentures, was offset on January 1, 2006, from the balance of the convertible debentures as reported in the balance sheet as of December 31, 2005.

This Standard does not apply to liabilities deriving from insurance contracts.

4. Initial adoption of Accounting Standard No. 24 regarding share-based payment

On January 1, 2006, the Company adopted the provisions of Accounting Standard No. 24, Share-Based Payment"(hereunder - the Standard) of the Israel Accounting Standards Board. The Standard prescribes rules for measurement and other requirements for three types of share-based transactions:

NOTES TO THE FINANCIAL STATEMENTS

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

- b. Initial adoption of new Accounting Standards (Cont.)
 - 4. Initial adoption of Accounting Standard No. 24 regarding share-based payment (Cont.)
 - a) Equity-settled share-based payment transactions;
 - b) Cash-settled share-based payment transactions;
 - c) Share-based payment transactions which allow the entity or counterparty to choose the manner of settlement.

For equity-settled share-based payment transactions, the Standard is applicable to grants made subsequent to March 15, 2005, and which had not yet vested as of January 1, 2006. The Standard is also applicable to modifications that were made to the terms of equity-settled transactions subsequent to March 15, 2005, even if the modifications relate to grants that were made before this date. In the financial statements for 2006, comparative data in the financial statements for 2005 are to be restated in order to reflect the expense relating to the aforementioned grants.

The Standard applies to all transactions in which a share-based payment is made in respect of purchase of goods or services, including transactions with employees or other parties that must be settled using the Company's equity instruments or in cash. Recording the expense in the statements of profit and loss will be against an increase when the share-based payment transaction is settled in equity instruments, or a liability is recorded when the transaction is settled in cash.

As a result of the initial adoption of the provisions of the Standard:

- a) The Company recorded for the three months ended March 31, 2006, an expense in the statement of profit and loss and a corresponding increase in shareholders' equity that was allocated to the capital reserves in the amount of about NIS 1,311 thousand in respect of option allotment.
- b) The Company restated its financial statements for the year ended December 31, 2005, in order to retroactively reflect the effect of the change in accounting treatment of share-based payment transactions with employees or other parties, to be settled using the Company's equity instruments, and which had been granted subsequent to March 15, 2005 and had not vested as of December 31, 2005.

NOTES TO THE FINANCIAL STATEMENTS**NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)**b. Initial adoption of new Accounting Standards (Cont.)4. Initial adoption of Accounting Standard No. 24 regarding share-based payment (Cont.)

Hereunder is the effect of the changes on the financial statements:

In the balance sheet

	<u>As at December 31, 2005</u>		
	<u>As previously reported</u>	<u>The change</u>	<u>As presented in these financial statements</u>
	<u>Reported NIS in thousands</u>		
Capital reserves	58,345	230	58,575
Retained loss	55,906	230	56,136

In the statements of profit and loss

	<u>Year ended December 31, 2005</u>		
	<u>As previously reported</u>	<u>The change</u>	<u>As presented in these financial statements</u>
	<u>Reported NIS in thousands</u>		
Cost and expenses in insurance business	(801,684)	(350)	(802,034)
The minority's share in subsidiary's profits	(26,988)	120	(26,868)
Income before taxes on income	73,943	(350)	73,593
Loss for the year	(11,076)	(230)	(11,306)

5. Initial adoption of Accounting Standard No. 25 regarding revenues

On January 1, 2006, the Company adopted the provisions of Accounting Standard No. 25, Revenues (hereunder - the Standard) of the Israel Accounting Standards Board. The Standard deals with the recognition of revenue from three types of transactions: sale of goods, rendering of services and revenue from interest, royalties and dividends and prescribes the required accounting treatment (principles of recognition, measurement, presentation and disclosure) regarding these three types of transactions.

The initial adoption of the Standard had no effect on the interim financial statements.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 3:- DATA REGARDING THE ISRAELI CPI AND THE FOREIGN CURRENCY EXCHANGE RATES

As at	Israeli CPI in points *)	Representative exchange rate of U.S. dollars	Representative exchange rate of Canadian dollars	Representative exchange rate of Pound Sterling NIS	Representative exchange rate of Euro	Representative exchange rate of Zolty
March 31, 2006	110.0	4.665	4.020	8.127	5,662	1.442
March 31, 2005	106.8	4.361	3.596	8.206	5.649	1.379
December 31, 2005	185.1	4.603	3.964	7.941	5.447	1.411
Rate of change during the period	%	%	%	%	%	%
March 2006 (three months)	0.6	1.3	1.4	2.3	3.9	2.3
March 2005 (three months)	(0.6)	1.2	0.5	(1.2)	(3.9)	(4.9)
December 2005 (12 months)	2.4	6.08	10.8	(4.4)	(7.3)	(2.8)

*) The CPI is at the average basis of 2000 = 100.

NOTE 4:- INFORMATION ACCORDING TO BUSINESS SEGMENTS

	Three month period ended March 31, 2006					Total
	Insurance	Leasing of assets	Asset management and stock exchange services	Others	Adjustments	
	Reported NIS in thousands					
Income from external source	219,841	32,807	2,457	-	-	255,105
Inter-company income	-	693	-	1,254	(1,947)	-
Capital gain and other income	36	5,845	-	-	-	5,881
Total	219,877	39,345	2,457	1,254	(1,947)	260,986
Segment results	13,868	8,189	(3,833)	(8,004)		10,220

NOTES TO THE FINANCIAL STATEMENTS**NOTE 4:- INFORMATION ACCORDING TO BUSINESS SEGMENTS (Cont.)**

	Three month period ended March 31, 2005					Total
	Insurance	Leasing of assets	Asset management and stock exchange services	Others	Adjustments	
			Reported NIS in thousands			
Income from external source	209,673	27,210	3,190	2,928	-	243,001
Inter-company income	-	714	-	1,358	(2,072)	-
Capital gain and other income	(351)	5,598	-	1,802	-	7,049
Total	209,322	33,522	3,190	6,088	(2,072)	250,050
Segment results	16,320	10,076	(1,029)	(2,914)		22,453

	Year ended December 31, 2005					Total
	Insurance	Leasing of assets	Asset management and stock exchange services	Others	Adjustments	
			Reported NIS in thousands			
Income from external source	886,908	114,642	11,462	2,928	-	1,015,940
Inter-company income	-	2,835	-	5,494	(8,329)	-
Capital gain and other income	4,273	7,056	-	-	-	11,329
Total	891,181	124,573	11,462	8,422	(8,329)	1,027,269
Segment results	84,664 *	22,388	(10,065)	(23,394)		73,593

*) Restatement – see Note 2b(4).

NOTE 5:- SIGNIFICANT EVENTS DURING THE REPORTING PERIOD

- a. During the reporting period the Company allotted in a private issue, NIS 50,000 thousand nominal value debentures (Series E), in consideration for NIS 54,615 thousand (net of issue expenses). The debentures allotted have the same terms as the debentures (Series E) that were issued by the Company in accordance to the prospectus from August 23, 2005.

The debentures are linked to the CPI and bear linked interest at the rate of 5.6% per annum. The debentures will be settled in six equal annual payments, in April 30 of each of the years from 2008 up to and including 2013. The interest will be paid each year beginning from April 30, 2006.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 5:- SIGNIFICANT EVENTS DURING THE REPORTING PERIOD (Cont.)

- b. During February 2006 an agreement was signed between Direct Investment House (Mutual Funds) Ltd. (hereunder – Direct Mutual Funds), which is a company wholly owned by the subsidiary, Direct Insurance Financial Investments Ltd. (hereunder – Direct Insurance), and between Bank Massad Ltd. and Bank Yahav for State Workers Ltd. (hereunder – the banks) for the acquisition of the activities of 17 mutual funds that were managed by the banks. The transaction was subject to the approval of the banks board of directors and an approval by the Controller of the Restrictive Trade Practices. The approvals were received by the end of March 31, 2006 and the activities were passed on to be managed by Direct Mutual Funds on April 4, 2006.

The consideration for the acquisition of the activities and related acquisition expenses amounted to about NIS 56 million (of this, about NIS 16 million was paid at the beginning of April 2006).

In order to finance the acquisition of activities, Direct Mutual Funds received a loan in the amount of NIS 50 million linked to the CPI and bearing annual interest at the rate of 5.25% which is repaid every 6 months. The loan will be settled in 7 equal installments beginning from April 14, 2009.

Direct Insurance and its subsidiary signed a guarantee limited to the amount of the loan as a collateral for its settlement.

- c. During the reporting period a subsidiary, Adgar, acquired a commercial center in Petach Tikva, on an area of 6,600 square meters at the cost of about \$ 13.5 million. About 96% of the center is leased and is expected to generate leasing income in the amount of about \$ 1.2 million, in addition to the expansion of the structure into an office structure.
- d. During the reporting period a wholly owned subsidiary of Adgar sold the office building it owned in Belgium in consideration for about NIS 9 million. In respect of the sale, a net profit after taxes in the amount of about NIS 6 million was recorded.
- e. During the reporting period a wholly owned subsidiary of Adgar signed an agreement to sell an office building in its ownership in London in consideration for about 13.5 million Pounds Sterling. The transaction is set to be completed on May 3, 2006. The expected capital gain, net, after deduction of costs involved in the transaction will amount to about 3 million Pounds Sterling (about NIS 25 million).
- f. In March 2006, Adgar issued NIS 80,000 thousand nominal value debentures (Series D) in consideration for NIS 87,579 thousand (net of issue expenses). The debentures have the same terms as the debentures (Series D) that were issued in the year 2004. The debentures bear the interest of 6.35% per annum, linked to the CPI.

The debentures principal will be settled in 7 installments beginning from August 2007 up to and including 2013 and the interest will be settled each year in August beginning from the year 2006 up to and including the year 2013.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 5:- SIGNIFICANT EVENTS DURING THE REPORTING PERIOD (Cont.)

- g During March 2006 Adgar decided to make an allotment of 1,800,000 of its ordinary shares of NIS 1 nominal value in favor of K.H.L. Educational Fund for Employees Ltd., for provident funds and/or an educational fund it manages. The total net proceeds, net of issue expenses, amounted to about NIS 8,155 thousand. As a result of the issue the Company's holdings in Adgar decreased from 71% to 69%. The capital gain that was recorded amounted to about NIS 0.5 million.
- h. During the reporting period 25,091 capital notes (Series C) were converted to 11,405 preferred shares of NIS 1 nominal value.

NOTE 6:- EVENTS AFTER THE BALANCE SHEET DATE

- a. In March 2006, the Company announced its intention to consolidate the authorized share capital and the issued and paid-up share capital to include only ordinary shares of NIS 1 nominal value each, with equal rights. The shares were consolidated by converting each preferred share into an ordinary share, at the ratio of 1:1 and without granting any compensation whatsoever to the holders of ordinary shares and/or to the holders of preferred shares and/or to any specific shareholders. During April the general meetings of holders of shares and capital notes approved the capital consolidation.
- b. In May 2006 a 75% held subsidiary of Adgar sold an office building in its ownership on Lyman Street in Great Britain, in consideration for about 31.4 million Pounds Sterling (about NIS 260 million).

The expected net capital gain, after the deduction of all costs involved in the transaction, will amount to about 8.5 million Pounds Sterling (about NIS 71 million). The Company's share in the expected capital gain, net, will amount to about NIS 40 million.

The transaction will be completed during June 2006.

- c. On March 30, 2006, the Company's board of directors decided to allot, in the framework of a private issue to an unrelated party, 1,600,000 ordinary shares of NIS 1 nominal value each (which constitute about 2.57% of the issued and paid-up share capital) and 1,000,000 options (Series 8) convertible to ordinary shares of NIS 1 nominal value each in consideration for the realization price of NIS 8.3 for each option (fully diluted, the securities that were issued, constitute about 3.87% of the share capital). The options are linked to the CPI and are realizable up to May 31, 2009. Any option warrant that is not realized up to the end of the realization period, will expire and the holders will not have any rights whatsoever in them. The proceeds from the issue amounted to about NIS 10,592 thousand.
