

**CLAL INDUSTRIES AND INVESTMENTS LTD.**

**MANAGEMENT DISCUSSION AND ANALYSIS**

**AS OF JUNE 30, 2000**

# **CLAL INDUSTRIES AND INVESTMENTS LTD.**

## **MANAGEMENT DISCUSSION AND ANALYSIS DECEMBER 31, 1999**

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### **1. Description of the Company**

Clal Industries and Investments Ltd., (“CII” or “the Company”) is an investment company, whose principal holdings are in the manufacturing and high-technology industries. As a result of the merger of Clal (Israel) and IDB Development Corporation Ltd., the Company is currently held directly by IDB Development Corporation Ltd.

CII is principally engaged in the acquisition, establishment and development of companies in various industries and takes an active role in the management of its investee companies, in particular when it is the largest investor.

The CII group of companies are engaged in a variety of segments, which primarily include: high-technology, electronics, biotechnology, communications, management of venture capital funds, infrastructure, paper and textile.

New investments are in four principal fields of specialization: biotechnology, software, semi-conductor equipment and communication technologies.

The Company views its contribution and assistance to the community as a vital component of its visionary business plan.

### **2. Results of Operations**

#### **A. Net income**

Net income for the second quarter amounted to NIS 117 million as compared with NIS 54 million in the corresponding quarter in the prior year. Net income for the quarter includes the effects of non-recurring net positive items amounting to NIS 83 million principally from the sale of Clalcom’s holdings in Med-1 in the amount of NIS 53 million. In the corresponding quarter last year the effects of non-recurring net positive items were in the amount of NIS 6 million.

Net income for the period under review amounted to approximately NIS 162 million in comparison to NIS 298 million in the corresponding period in the previous year and NIS 430 million for all of 1999. Net income for the reported period includes capital gains and the effects of non-recurring net positive items amounting to NIS 105 million in comparison to NIS 208 million in the corresponding period last year.

The principal decrease in current income for the quarter stems from the write down of Clal Capital Venture Fund’s investment, an increase in financing expenses and the increase in the amortization of goodwill. These effects were partly offset by an increase in the Company’s share in Mashav and an increase in Kitan’s revenues.

As a result of the completion of the merger of the advanced printing product division of Scitex with Creo, Scitex included a gain of approximately NIS 512 million in its financial statements, based on the fair value of Creo shares registered for trading. The aforementioned gain is net of depreciation, research and development in progress expenses and tax effects.

The financial statements of Scitex are prepared in accordance with U.S. accounting standards and include a gain of NIS 470 million for the second quarter of the year. The Company includes its investment in Scitex on an equity basis, based on the financial statements of Scitex following the adjustment to Israeli accounting principles. As a result of this adjustment income to Israeli accounting principles, as interpreted by the Israeli Securities Authority, Scitex contributed a loss of NIS 5 million for the quarter to the Company.

The Board of Directors of the Company believes that the non-adjustment of accounting principles in Israel to accounting principles in the United States, as interpreted above, does not contribute to the development of the capital market in Israel and its adaptation to the process of globalization.

*B.* The following is a review of the activities of the principal investee companies in the second quarter:

- **Nesher:** There was a reduction in the sale of cement (2%) in comparison to the corresponding period last year as a result of the continued erosion of prices (4%) which was set off by an increase in the volume of cement sold. Net income of companies in the cement sector amounted to NIS 43 million as compared to NIS 42 million last year.
- **ECI:** Net income for the second quarter of the year was NIS 27 million (including a non-recurring expense in the amount of NIS 117 million with respect to the acquisition of research and development in progress expenses) as compared to NIS 219 million in the corresponding quarter in the prior year. Sales in the quarter increased by 17% and amounted to NIS 1,296 million in comparison to NIS 1,109 million in the corresponding quarter in the prior year. ECI announced its intention to split the Company into five separate companies in order to accelerate their growth and increase shareholders' equity.
- **AIPM:** Net income for the second quarter amounted to NIS 15 million, as compared to NIS 19 million in the corresponding quarter in the prior year. Income from the corresponding quarter in the prior year includes non-recurring profits in the amount of NIS 6 million. The increase in current profit was due to an increase in activities in all areas which was partly set off by an increase in the price of raw materials.

- **Kitan:** Net income for the second quarter amounted to NIS 7 million, as compared to NIS 1 million in the corresponding quarter in the prior year. The principal increase in income was due to an improvement in the results of the Golf-Kitan chain of stores. The Golf-Kitan chain of stores has submitted a draft prospectus to the Securities Authority.
- **Polgat:** The company reported a decrease in net income from NIS 16 million for the corresponding quarter last year to a break even this year. This decrease in income stems mainly from a decrease in sales, primarily due to the erosion of sales prices to central customers and the revaluation of the dollar against the British pound. In the reported period, Polgat accelerated the transfer of production operations outside of Israel as part of the measures taken to significantly decrease production costs during 2001. Polgat Textiles is conducting negotiations with the Turkish Group - Guney Sanayi with respect to the merger of the companies.
- **Barak:** The increase in revenues continued reaching NIS 126 million for the second quarter, as compared to NIS 98 million in the corresponding quarter last year. Barak completed the current quarter with a gross profit of NIS 19 million as compared to a gross loss of NIS 3 million in the corresponding quarter in the prior year. Net loss for the second quarter decreased to NIS 24 million as compared to NIS 41 million in the corresponding quarter in the prior year. For the first time, in the second quarter Barak transferred over to a positive EBIDTA of NIS 1.3 million.
- **Fundtech:** Income for the quarter increased by 25% from NIS 37 million last year to NIS 46 million in the current quarter. The increase in operating expenses and particularly in research and development expenses of NIS 7 million, caused a decrease in net income before a non-recurring expense from NIS 10 million last year, to NIS 5 million in the current quarter.

C. The following is selected data from the financial statements of the principal investee companies (in millions of shekels - rounded):

	Sales (*)				Net Income (Loss)(**)			
	For the six months ended June 30		For the three months ended June 30		For the six months ended June 30		For the three months ended June 30	
	2000	1999	2000	1999	2000	1999	2000	1999
CEI	40	32	21	16	19	571	-	30
Mashav	830	870	451	449	72	81	47	45
Kitan	360	360	183	158	12	10	7	1
AIPM (***)	441	744	125	364	49	33	15	19
Barak	233	191	126	98	(69)	(76)	(24)	(41)
Polgat (***)	245	311	120	140	3	27	-	16
Fundtech	87	69	46	37	1	5	5	(2)

(\*) Relates to sales only and does not include CII's equity in the earnings of associated companies and other income, net.

(\*\*) Net income (loss) includes the effect of non-recurring transactions.

(\*\*\*) 1999 includes those companies whose consolidation was terminated in 2000.

D. *Earnings per share*

Earnings per NIS 1 par value share for the reported period was NIS 1.15, as compared with NIS 2.12 for the corresponding period in the prior year and NIS 3.06 for all of 1999.

E. *Return on shareholders' equity*

The rate of return on shareholders' equity for the quarter was approximately 10.3% as compared with 20.6% for the corresponding quarter in the prior year and 15.3% for all of 1999.

### **3. *Financial Position***

- A.* Total assets in the consolidated balance sheet of the Group as of June 30, 2000, amounted to NIS 7,635 million, as compared with NIS 5,559 million at the end of the corresponding period last year and NIS 6,268 at the end of 1999.

The principal increase in the consolidated balance sheet as of June 30, 2000 stems from the full inclusion of the assets and liabilities of Mashav, as a result of the acquisition of 50% thereof in January 2000.

Due to the external financing sources of the investment in Mashav, the Company incurred a deficit in working capital of approximately NIS 1 billion.

### **4. *Principle Changes in Investments***

- A.* In January 2000, the Company acquired all of Koor Industries' holdings in Mashav in consideration for NIS 893 million. On completion of the transaction, the Company's holding in Mashav increased to 100%. The acquisition was financed by the increase in the Company's external sources of financing.
- B.* In January 2000, Clalcom sold 8.2% of Med-1's capital to Telecom, Italy in consideration for NIS 80 million. Net gain from the transaction amounted to NIS 53 million. The balance of Clalcom's holding in Med-1, as well as in Med Nautilus (the Company which coordinates the international cable activities of Med-1's shareholders') is 15%.
- C.* In April 2000, Scitex completed an agreement for the merger of its pre-printing operations with those of the Canadian Company, Creo. On completion of the transaction, Scitex holds 26% of the share capital of Creo. With respect to the effect of the merger on the Company's results - see paragraph 2A.
- D.* In March 2000, Clal Electronics Industries Ltd. ("CEI") invested NIS 51 million in debentures convertible into shares of Orchit.
- E.* In March 2000, the Company invested NIS 30 million in the shares of Orsus, subsequent to which the Company's holdings in Orsus increased to 18.5%.
- F.* In March 2000, CEI converted ECI's convertible debentures into shares. As of June 30, 2000, CEI's holding in ECI increased to 13.8%.
- G.* In March 2000, the Company sold part of its holdings in BVRT in consideration for NIS 11 million. The Company recorded a gain of NIS 8 million.

- H.* In April 2000, Nova raised NIS 201 million in an initial public offering in the U.S. As a result of the issuance, CEI's holdings in Nova decreased to 19.8% generating capital in the amount of NIS 21 million.
- I.* In April 2000, the Company made a commitment to invest \$10 million in the Carmel Fund, of which the Company's actual investment is \$ 1 million.
- J.* In May 2000, the Company sold all its holdings in Sunfrost in consideration for \$4 million. As a result of the sale, the Company recorded a gain of NIS 9 million.
- K.* A wholly owned subsidiary of the Company received an additional consideration with respect to the sale of PRI shares in June 1998. As a result thereof, the Company recorded a gain of NIS 7 million.
- L.* During May through August, a wholly owned subsidiary acquired 7.8% of Med Yavne and Med Ashdod's petroleum and gas license for an aggregate amount of NIS 16 million. This investment was implemented concurrently with the acquisition by other partners of 7.2% of Mediterranean Energy.

At drilling site Nir 1, a layer approximately 300 meters thick was found which includes a number of sandy sections as well as sections of sand and sediment containing gas. At this stage the data received is being analyzed and upon completion, it will be possible to estimate the potential productivity of the site.

- M.* In August, Compugen raised NIS 200 million in the framework of an initial public offering in the U.S. Subsequent to the offering, CIB's holdings in Compugen reached 12.1%.
- N.* In the reported period, the Company undertook together with CEI (in equal parts) to invest in Star (\$5 million) and Genesis II (\$6 million) capital venture funds. In addition the Company, together with CEI (in equal parts) invested \$6 million in convertible debentures of Viryanet Ltd. and \$5 million in Cellastra Ltd.

##### ***5. Report on preparation for the Y2K Issue***

No changes.

##### ***6. Analysis of exposure to market risks and the management thereof***

No changes.

## **7. Assistance to the Israeli Community**

CII views its contribution and assistance to the community as a vital component of its visionary business plan. This activity is implemented, amongst others, by the “Clal Fund” Foundation jointly with the parent company and the Group companies and has been operational for the past 17 years to assist those in need, institutions as well as educational, cultural, art and health institutes. Commencing in 1998, in the framework of the IDB Group and in cooperation with the University of the Negev, the Company has adopted a special social project - an open housing program in three neighborhoods of Beer Sheva. The Company encourages the Group companies to intensify their activities in the framework of “Business for the Community” projects which leads the “Zionism 2000” movement.

As of today, the Group companies have adopted 19 projects addressed mainly to underprivileged population groups. Concurrently and in addition thereto, the Tapuach Foundation was established at the initiative of the IDB Group and with the participation of the Company and its subsidiaries, for the promotion of information in Israel. The Foundation operates as a not for profit institution in cooperation with institutional agents, the aim thereof being to train the general public for Internet utilization and the acquisition of technological skills while focusing on underprivileged neighborhoods, development towns and minority settlements.

The Foundation’s long term program includes the establishment of 30 community centers where education and supervision is provided in the area of technological information including “Basic English Internet” at an aggregate budget of NIS 40 million. The first Tapuach Center was opened on August 1, 2000 in Mitzphe Ramon.

We wish to express our gratitude to the managers and employees of the Group for their contribution to the progress and development of the Group.

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**LEON RECANATI**  
Chairman of the Board

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**RIMON BEN-SHAOUL**  
General Manager

Tel-Aviv, August 22, 2000

**CLAL INDUSTRIES AND INVESTMENTS LTD.**

**SELECTED CONSOLIDATED FINANCIAL DATA  
AS OF JUNE 30, 2000  
(Unaudited)**

# CLAL INDUSTRIES AND INVESTMENTS LTD.

## SELECTED CONSOLIDATED BALANCE SHEET DATA

In thousands of shekels of June 2000

	<b>June 30</b>		<b>December 31</b>
	<b>2000</b>	<b>1999</b>	<b>1999</b>
	<b>(Unaudited)</b>		<b>(Audited)</b>
<u>Assets</u>			
Current assets	1,617,236	1,488,022	1,880,713
Deposits, long-term loans and debts	92,038	169,402	92,574
Investments	3,144,071	2,386,575	2,800,674
Fixed assets, other assets and differed charges	<u>2,781,396</u>	<u>1,514,642</u>	<u>1,494,473</u>
	<u>7,634,741</u>	<u>5,558,641</u>	<u>6,268,434</u>
<u>Liabilities and Shareholders' Equity</u>			
Current liabilities	2,667,313	1,043,647	1,694,998
Long-term liabilities	789,774	582,230	528,878
Minority interests	902,975	927,527	901,597
Shareholders' equity	<u>3,274,679</u>	<u>3,005,237</u>	<u>3,142,961</u>
	<u>7,634,741</u>	<u>5,558,641</u>	<u>6,268,434</u>

## CLAL INDUSTRIES AND INVESTMENTS LTD.

### SELECTED CONSOLIDATED STATEMENT OF INCOME DATA

In thousands of shekels of June 2000

	<b>For the six months ended June 30</b>		<b>For the three months ended March 31</b>		<b>For the year ended December 31</b>
	<b>2000</b>	<b>1999</b>	<b>2000</b>	<b>1999</b>	<b>1999</b>
	<b>(Unaudited)</b>		<b>(Unaudited)</b>		<b>(Audited)</b>
Revenues, net	1,736,937	1,390,776	924,456	451,820	2,689,872
Costs and expenses	1,490,026	800,080	756,946	374,755	1,896,718
Income before taxes on income	246,911	590,696	167,510	77,065	793,154
Taxes on income	71,765	28,250	53,530	14,117	48,014
Income after taxes on income	175,146	562,446	113,980	62,948	745,140
Minority interests	13,291	263,942	(3,416)	8,927	314,997
Net income	161,855	298,504	117,396	54,021	430,143
Earnings per share (in shekels)	1.15	2.12	0.84	0.39	3.06