

Clal Industries and Investments Ltd.

MANAGEMENT DISCUSSION AND ANALYSIS

For the Period January-June 2004

1. **Company Description**

Clal Industries and Investments Ltd. ("CII") is an investment company, whose principal holdings are in the manufacturing and high-technology industries. The Company is controlled by IDB Development Corporation Ltd.

The Company – on its own and through its subsidiaries – deals in the establishment, acquisition, development and upgrading of companies in various industries. The Company strives to be involved in the management and steering of its investee companies, primarily when the Company possesses significant holdings in these companies. The Company strives to enhance and maximize the value of its existing investments, with a view to realizing those investments at the appropriate time. The Company has access to a variety of business opportunities, being constantly alert for investments with a suitable potential return, in those sectors where it is experienced and knowledgeable.

The CII group of companies is actively engaged in a variety of sectors, including primarily: Cement, high technology and electronics, venture capital, paper and cardboard, textile, biotechnology, transportation, logistics and communications.

The Company operates according to basic principles that were approved in the past by the Board of Directors, calling for long-term business deployment. The basic principles include focusing on a limited number of material holdings possessing growth potential, in whose upgrading the Company can exert a significant influence, an emphasis on the development of management resources, focus on investments in rapid growth sectors, while providing support and encouraging long-term strategic processes in the investee companies. These measures and processes are constantly being evaluated and adapted. The Company consequently adapts its operational profile while adopting advanced management and business tools.

As a result of the adoption of the basic principles, the Company's investments were classified into four groups: Principal holdings, venture capital, biotechnology and other real holdings.

The Company's operations are performed through subsidiaries (companies in which the Group holds 50% or more of the rights, either directly or indirectly), through associated companies (companies in which the Group exercises significant influence and which are accounted for by the equity method), and through other companies wherein the Company does not exercise significant influence (the investment in which is reflected in the financial statements on a cost basis).

The Company's financial results are affected, to a significant extent, by earnings from the realization of investments and write-downs. Accordingly, significant fluctuation may be recorded in the Company's results of operations between the various reporting periods.

The Company views contributions to the community as a central tier in its business vision.

2. **Results of Operations**¹

- A. The Company's net income in the reported period amounted to NIS 256 million, as compared with a loss of NIS 206 million in the corresponding period last year.

The net income for the period includes earnings of NIS 222 million from the realization of investments, net of write-downs (primarily the realization of investments at Ormat – NIS 128 million; SDP – NIS 57 million; Negevtech – NIS 33 million; PowerDsine – NIS 23 million; Opticanada – NIS 14 million and the impairment of the investment in Shellcase – NIS 18 million), coupled with positive non-recurring factors totaling NIS 26 million (primarily the impact of the lowering of the corporate tax rate – NIS 35 million). The corresponding period last year included a loss of NIS 138 million on account of write-downs net of earnings from the realization of assets, coupled with negative non-recurring factors totaling NIS 10 million.

The transition to current earnings for the period, as compared with the corresponding period last year, originates from an improvement in most of the principal investee companies (primarily Neshet, Kitan and Scitex), that was partially offset by higher financial expenses.

The Company's net income in the second quarter amounted to NIS 88 million, as compared with a loss of NIS 123 million in the second quarter last year and a loss of NIS 129 million for all of 2003.

¹ According to Israeli financial standards, the adjustment of financial statements was discontinued starting January 1st 2004. The comparison figures for preceding periods are presented adjusted to the NIS of December 2003. The rules were also modified regarding the inclusion of the financial statements and results of operation of investee companies whose operating currency differs from the operating currency of the Company. (See also Note 2b to the Financial Statements).

The net income for the quarter includes earnings of NIS 52 million from the realization of investments, net of write-downs (primarily the realization of investments at Negevtech – NIS 33 million; PowerDsine – NIS 23 million; Ormat – NIS 15 million; Opticanada – NIS 14 million and the impairment of the investment in Shellcase – NIS 18 million due to the downturn in the state of its business), coupled with positive non-recurring factors totaling NIS 26 million (primarily the impact of the lowering of the corporate tax rate – NIS 35 million). The corresponding quarter last year included a loss of NIS 99 million on account of write-downs net of earnings from the realization of assets, coupled with negative non-recurring factors totaling NIS 8 million.

The transition to current earnings (net income net of earnings from the realization of investments, write-downs and non-recurring factors) during the quarter, as compared with the corresponding quarter last year originates from improved results at most of the principal companies (primarily Neshet and Scitex), that were partially offset by growth in financial expenses.

The net income per NIS 1 par value of shares in the reported period amounted to NIS 1.63, as compared with a loss of NIS 1.31 in the corresponding period last year and a loss of NIS 0.82 for all of 2003.

The following is an analysis of the financial results (in NIS millions):

	For the three months ended June 30 th 2004			For the three months ended June 30 th 2003		
	Current	Other ²	Total	Current	Other ²	Total
Principal holdings	50	81	131	18	(29)	(11)
Venture capital	(2)	5	3	(1)	(30)	(31)
Biotechnology	(10)	(1)	(11)	(10)	(32)	(42)
Other real holdings	7	(7)	-	1	(6)	(5)
Headquarters	(4)	-	(4)	-	(10)	(10)
Financing	(31)	-	(31)	(24)	-	(24)
Net Income (loss)	<u>10</u>	<u>78</u>	<u>88</u>	<u>(16)</u>	<u>(107)</u>	<u>(123)</u>

² Including results of the realization of investments, impairment of investments and non-recurring factors.

	For the six months ended June 30 th 2004			For the six months ended June 30 th 2003		
	Current	Other ²	Total	Current	Other ²	Total
	Principal holdings	72	270	342	(4)	(46)
Venture capital	(6)	(1)	(7)	(5)	(48)	(53)
Biotechnology	(21)	(14)	(35)	(25)	(38)	(63)
Other real holdings	10	(7)	3	7	(6)	1
Headquarters	(6)	-	(6)	(2)	(10)	(12)
Financing	(41)	-	(41)	(29)	-	(29)
Net Income (loss)	<u>8</u>	<u>248</u>	<u>256</u>	<u>(58)</u>	<u>(148)</u>	<u>(206)</u>

B. Data Regarding Principal Investee Companies³

The following are data from the financial statements of the principal investee companies. The data are presented according to the operating currency of each company (in millions):

	<u>Sales</u>				<u>Net Income (loss)</u> ⁴			
	For the six months ended June 30 th		For the three months ended June 30 th		For the six months ended June 30 th		For the three months ended June 30 th	
	<u>2004</u>	<u>2003</u>	<u>2004</u>	<u>2003</u>	<u>2004</u>	<u>2003</u>	<u>2004</u>	<u>2003</u>
Companies whose financial statements are in NIS:								
Mashav	732	658	385	360	99	7	71	25
Kitan	394	372	185	176	4	(5)	(1)	(1.5)
AIPM	238	233	119	115	43	31	25	18
Barak	354	323	161	162	(80)	65	9	46
Companies whose financial statements are in US dollars:								
ECI ⁵	\$229	\$195	\$121	\$92	(\$5)	(\$43)	(\$4)	(\$35)
Scitex ⁵	\$60	\$48	\$31	\$25	\$49	(\$12)	(\$1)	(\$5)
Polgat	\$96	\$82	\$50	\$44	\$2	\$2	\$1	\$2
Fundtech	\$27	\$23	\$14	\$12	\$0.6	(\$0.9)	\$0.4	(\$0.2)

²Including results of the realization of investments, impairment of investments and non-recurring factors.

³ The review of ECI, Scitex and Fundtech is based on financial statements prepared in accordance with accounting principles generally accepted in the United States.

⁴ Net income (loss) includes non-recurring items.

⁵ The comparison figures were adjusted in order to reflect discontinued operations.

C. Contribution to Earnings from Principal Investee Companies (in NIS millions):

	For the six months ended June 30 th		For the three months ended June 30 th	
	<u>2004</u>	<u>2003</u>	<u>2004</u>	<u>2003</u>
Mashav	74	5	54	19
Kitan	4	(5)	(1)	(1.5)
AIPM	13	11	8	6
ECI	-	(27)	1	(19)
Scitex	58	(13)	3	(5)
Polgat	7	7	4	6
Fundtech	-	(3)	-	(1)

D. Review of Operations of Principal Companies in the Second Quarter ⁶

Nesher – An increase was recorded in revenues from sales (3%) during the second quarter, as compared with the corresponding quarter last year, primarily as a result of growth in the quantities sold to exports. The quarterly earnings (prior to positive non-recurring factors totaling NIS 31 million, thanks to changes in deferred taxes, primarily due to the change in the corporate tax rate in Israel) amounted to NIS 36 million, as compared with earnings of NIS 26 million in the corresponding quarter last year. The improved profitability originated primarily from the decrease in manufacturing costs, thanks to efficiency measures that were initiated in 2003.

ECI⁷ – The gross profit for the quarter amounted to \$49 million (gross margin = 41%), as compared with \$34 million (gross margin = 37%) in the corresponding quarter last year. The operating income for the quarter amounted to \$5 million, as compared with an operating loss of \$21 million in the corresponding quarter last year. The income from ongoing operations for the quarter amounted to \$2 million, as compared with a loss of \$26.5 million in the corresponding quarter last year.

The improvement in the ECI operations was reflected in ECI's two principal areas of operation – products for broadband and optical telecommunications equipment. The broadband access division recorded revenues of \$51 million for the quarter, representing growth of 14% as compared with the corresponding quarter last year. The division's operating income amounted to \$5 million, as compared with \$4 million in the corresponding quarter last year.

The revenues of the optical networks division grew to reach \$61 million for the quarter, up from \$40 million in the corresponding quarter. The division made the transition to operating income of \$1 million, as compared with a loss of \$15.5 million in the corresponding quarter last year, after four years of losses.

⁶The review of ECI, Scitex and Fundtech is based on financial statements prepared in accordance with accounting principles generally accepted in the United States.

⁷The comparison figures were adjusted in order to reflect discontinued operations.

On May 10th 2004, ECI distributed to its shareholders most of its holdings in the ECTel share capital. Following the said distribution, the Company holds approximately 6% of the ECTel share capital. The company undertook not to sell the said shares for a period of one year from the distribution date. Starting with the distribution date, ECI no longer consolidates the ECTel financial statements.

Scitex⁷ – The quarterly sales amounted to \$31 million, as compared with \$25 million in the corresponding quarter last year (up 25%). The operating income for the quarter amounted to \$0.2 million, as compared with an operating loss of \$2 million in the corresponding quarter last year. The transition to operating profitability originated from the growth in sales and the improvement in gross profit. The loss for the quarter amounted to \$1 million, as compared with a loss of \$5 million in the corresponding quarter last year.

In January 2004, Scitex announced that it intends to distribute a sum of \$118 million to its shareholders, of which \$86 million will be in cash, while the remaining \$32 million are to be distributed by way of an independent acquisition of its own shares, through a special tender offer, pursuant to the Companies Law. On May 14th 2004, Scitex published a special detailed tender offer, pursuant to which Scitex acquired approximately 5 million of its own shares in June (representing approximately 11.5% of the Scitex issued share capital and voting rights, prior to the tender offer), in return for an overall sum of \$28 million. The Company, together with Discount Investments Ltd. (DIC), a subsidiary of the Company's parent company, sold 0.26 million Scitex shares as part of the tender offer.

Subsequent to the completion of the tender offer, the Company's holding rate in Scitex is equal to 24.7%. The overall holding rate (together with DIC) totals 49.1%.

In June, Scitex decided to distribute \$90 million to its shareholders. The distribution was made in July 2004. The Company's share in the distribution amounted to \$22 million.

AIPM – The operating income for the quarter amounted to NIS 14 million, as compared with NIS 10 million in the corresponding quarter last year. The quarterly net income (including positive, non-recurring income of NIS 10 million as a result of the change in the Israeli corporate tax rate) amounted to NIS 25 million, as compared with NIS 18 million in the corresponding quarter last year. The decrease in the current profit originated from the decrease in AIPM's share in the earnings of associated companies (originating primarily from lower financial revenues at Hogla-Kimberly and lower profitability at Ovisan in Turkey), that was partially offset by the decrease in financial expenses.

Kitan - The sales in the second quarter amounted to NIS 185 million, as compared with sales of NIS 176 million in the corresponding quarter last year. The operating income amounted to NIS 6 million for the quarter, as compared with operating income of NIS 5 million in the corresponding quarter last year. The improved operating income is attributed to the decrease in selling and marketing expenses and the decrease in general and administrative expenses, that were partially offset by the decrease in gross profit following the decrease in retail sales due to the timing of the Passover holiday. The loss for the quarter amounted to NIS 1 million and is similar to the loss in the corresponding quarter last year. This loss was affected by the growth in other expenses and the transition from financing expenses to financing revenues.

In May 2004, Kitan Industries joined a partner active in the household textile sector, in establishing a partnership dealing in the marketing, sale and distribution of household textile products in the United States (Kitan's share is 50%). The establishment of this partnership is expected to enable Kitan Industries to operate competitively in the American market. In parallel, Kitan Industries is developing new sources of manufacture for the European market.

Polgat – The quarterly sales amounted to \$50 million, as compared with \$44 million in the corresponding quarter last year. The growth in sales originated from Bagir (active in the formal menswear sector) and from growth in the sales of Guney Polgat (“GP”) (active in the manufacture of fabric and yarn) to the US market. The gross profit for the quarter amounted to \$11 million (gross margin of 22%), similar to the corresponding quarter last year (gross margin last year = 25%). The decrease in the gross margin is attributed to the sale of irregular stock by GP and was partially offset by an increase in the gross margin at Bagir, primarily on account of the growth in the sales to Marks & Spencer (M&S). The quarterly net income amounted to \$1 million, as compared with net income of \$2 million in the corresponding quarter last year. The decrease in net income originated primarily from the growth in the operating loss of GP, that was partially offset by a rise in Bagir's operating income.

At the end of the second quarter, Bagir was informed by its major client, M&S, that the latter would gradually be lowering its purchasing prices from Bagir, as part of its comprehensive move to lower costs and improve its profitability. Similar notice was sent to all of the M&S suppliers. Bagir estimates that this move will serve to lower its net income by \$1 million in 2004.

As part of Bagir's manufacturing strategy, the company signed a joint venture agreement with a Chinese company, for the establishment of a company in China. Furthermore, Bagir continued to reduce the number of employees at its Kiryat-Gat plant.

GP began implementing a work plan in 2003, with the intention of focusing the GP operations and rendering them more efficient, in view of the continuing losses at GP and its deteriorating working capital situation. The work plan is not being implemented in full, partly due to disagreements between Polgat and its Turkish partners regarding several crucial issues therein. Polgat and the Turkish partners are considering a restructuring program at GP. There is no certainty that any restructuring will take place and no committing agreement has been signed between the parties. GP's President resigned his position in May 2004. Two directors (one from each party) were appointed in his place, to accompany GP's management in the current operations.

Barak⁸ – The quarterly gross profit amounted to NIS 49 million (gross margin = 30%), as compared with gross profit of NIS 60 million (gross margin = 36%) in the corresponding quarter last year. The competition in the sector and the opening of the international, long-distance telephony market to additional operators has resulted in a sharp drop in gross profit due to the lowering of prices, coupled with an increase in marketing expenses that brought about a decrease in operating income in the second quarter, bringing operating income to NIS 16 million, as compared with NIS 31 million in the corresponding quarter last year. The net income in the current quarter amounted to NIS 9 million, as compared with NIS 46 million in the corresponding quarter last year. The lower net income is attributed to a sum of NIS 23 million in financing expenses, that resulted in a transition from financial revenues to financial expenses.

Fundtech – The net income for the reported period amounted to \$0.4 million, as compared with a loss of \$0.2 million in the corresponding period last year. The improvement in the quarterly profit originated primarily from a NIS 2 million increase in sales (up 17%) that was partially offset by growth in operating expenses (\$1.5 million), as compared with the corresponding quarter last year. 35 new deals were signed this quarter, as seven banks came on board as new customers.

Generally speaking, the results of the group companies during the reported period, were affected by the growth in demand on the local market, thanks to a slight growth in private consumption, coupled with relative calm in the security situation. It should be mentioned that the timing of the Passover holiday, that occurred in early April this year, adversely affected a number of investee companies that operate in the local market, during the second quarter. The Group companies operating in the hi-tech sector were affected by the continued growth in the acquisition of capital equipment overseas, which contributed to the growth in the volumes of sales of most of these companies. This growth in the volume of sales, along with the positive impact of the efficiency measures being implemented by most of the companies in the Group, have resulted in improved

⁸In accordance with generally-accepted accounting principles, the company provided for NIS 12 million on account of its investments in Barak (the provision was equal to NIS 11 million at Dec-31-03), in consideration of Barak's equity deficit and the guarantee provided by a subsidiary as part of the terms of the license received by Barak.

results.

Moreover, during most of the reported period, a recovery was evident in Israeli and global capital markets, which rendered possible the realization of investments and the raising of capital at Group companies. A downturn has recently been felt in Israeli and overseas capital markets. This fact will render it more difficult to raise capital and to realize investments.

During the reported period, the company as well as most of its principal investee companies have made the transition to financial reporting on a nominal basis. The results of the companies were consequently adversely affected by the rise in the inflation rate during the quarter. Additionally, the second quarter results were positively affected by the lowering of corporate tax rates in Israel.

2. **The Financial Situation and Sources of Finance**

The working capital in the consolidated balance sheets amounts to NIS 899 million. The short-term liquid assets in the consolidated balance sheets, as at the balance sheet date, amount to NIS 747 million and are included under the items short-term investments, cash and cash equivalents. The quick ratio in the consolidated balance sheets is equal to 1.14 (0.67 as at Dec-31-03). The principal cash sources originated from the issuing of NIS 540 million in debentures, the realization of investments in the sum of NIS 480 million, and the receipt of NIS 89 million in long-term loans. The cash sources were used primarily for the repayment of NIS 463 million in short-term loans, the repayment of NIS 111 million in long-term loans and the distribution of dividends in the sum of NIS 270 million.

As at June 30th 2004, the Company's shareholders' equity totaled NIS 2,018 million, as compared with NIS 2,008 million at December 31, 2003. The NIS 10 million growth in shareholders' equity is primarily attributed to the company's NIS 256 million in earnings during the period, coupled with a NIS 24 million increase in principal stemming from translation, net of distributed dividends of NIS 270 million. The minority interest amounted to NIS 343 million (NIS 95 million at Dec-31-03). On the sources side, the company's shareholders' equity rose (up 0.5%), along with the minority interests (up 261%), primarily as a result of the transition to full consolidation of Mashav, that was previously proportionately consolidated (see also Section 4.1, below) – that together financed 40% of the company's assets.

The Group's external long-term sources of finance totaled NIS 1,969 million at the end of the quarter (NIS 1,335 million as at Dec-31-03), approximately 13% of which are scheduled for repayment within the coming year.

The net outstanding liabilities of the Company and the wholly-owned subsidiaries as at June 30th 2004 amounted to NIS 785 million (NIS 930 million as at Dec-31-2003).

4. **Dividend**

On the date of approval of the financial statements, the Company's Board of Directors decided to distribute a cash dividend in the sum of NIS 250 million, representing NIS 1.59 for every NIS 1 par value of shares.

The dividend will be paid on September 27th 2004, with the determining date being September 12th 2004 and the X-date being September 13th 2004.

5. **Major Changes in Investments and in Investee Companies**

5.1 The option that was granted by the Company to CRH (Israel) Ltd. (hereinafter: "CRH"), within the framework of the agreement that was signed between the parties in August 2001, for the acquisition of an additional 25% of the share capital of Mashav Initiating and Development Ltd., held by the Company, expired on December 31, 2003 (hereinafter: "The Option"). In the course of the quarter, the company and CRH continued to negotiate for the sale of 25% of the Mashav shares. It was agreed that during the negotiations, the rights of the parties would be maintained, according to the arrangements that were in place during the option period. At the end of March 2004, the parties agreed that the rights for joint management that existed during the option period will not be extended. In the course of the second quarter, the Company and CRH agreed to discontinue their contacts for the sale of the additional 25% of Mashav shares.

Accordingly, during the first quarter of the year, the Company included – by proportionate consolidation (at a rate of 75%) – the Mashav statements of income. Starting March 31, 2004, Mashav's assets and liabilities, as well as its results of operation, are fully consolidated in the Company's financial statements. The addition to the consolidated assets as at March 31st 2004 amounts to approximately NIS 463 million and the supplemental net revenues from sales and services – for the period and for the second quarter – amount to NIS 96 million.

5.2 In January 2004, the Company sold all its holdings in Ormat shares in return for NIS 259 million. As a result of the sale, the Company recorded net earnings of NIS 113 million. In April 2004, the Company sold its holdings in convertible debentures and options for Ormat shares, in return for NIS 43 million. The Company recorded net earnings of NIS 15 million as a result of the sale.

5.3 In February 2004, the Company signed an agreement for the sale of all its holdings in Negevtech, in return for an immediate sum of NIS 65 million. Under certain conditions, derived from the cost of acquisition of additional Negevtech shares by the buyers, the Company may receive additional consideration. The transaction was finalized in May and given the immediate proceeds alone, the Company recorded net earnings of NIS 33 million.

- 5.4 In May 2004, the Company signed an agreement for the sale of half its holdings in PowerDsine (hereinafter: "PDSN"), in return for NIS 48 million. In June 2004, as part of the PSDN IPO, the Company sold approximately half of its remaining investment in return for NIS 25 million. The Company recorded net earnings of NIS 23 million as a result of these divestitures. As at June 30th, the Company holds 2.7% of the PDSN share capital.
- 5.5 In May 2004, the Company sold all its holdings in Opticanada Inc. in return for NIS 36 million. As a result of the sale, the Company recorded net earnings of NIS 14 million.
- 5.6 The Company made the following investments – both directly and indirectly (through wholly-owned subsidiaries) – in additional companies during the reported period, (in millions of adjusted shekels):

	For the six months ended <u>June 30, 2004</u>	For the three months ended <u>June 30, 2004</u>
Venture capital	19	13
Biotechnology	4	1
Total	<u>23</u>	<u>14</u>

- 5.7 Subsequent to the balance sheet date, in August 2004, Elron Electronic Industries Ltd. (hereinafter: "Elron") (a company in which DIC holds 46%) and Applied Radiation Jordan Valley Ltd. (hereinafter: "Applied Radiation"), a subsidiary of the Company (in which the Company holds 57%), signed an investment agreement in Applied Radiation. Pursuant to the investment agreement, Elron will invest a sum of \$6.7 million in return for 25% (fully diluted) of the share capital of Applied Radiation. The said transaction is contingent upon another transaction whereby the Company will convert shareholder loans totaling \$2.25 million into share capital of Applied Radiation, at terms that are similar to the terms of the Elron investment and upon settling the terms of the outstanding loans – in the sum of \$2 million – granted by the Company to Applied Radiation. Subsequent to the Elron investment and the conversion of the said company loans, the Company's holding rate in Applied Radiation will decrease to approximately 41% (fully diluted).

The final value of Applied Radiation for the purpose of the Elron investment, subsequent to the conversion of the loans by the Company, will be determined in July 2005, according to the performance of Applied Radiation and will lie in the range between \$10 and \$30 million. The Company's and Elron's holding percentage in Applied Radiation may change accordingly. Moreover, in the event that the final value of Applied Radiation shall be higher than \$20 million, Elron will be eligible to acquire additional shares, to ensure that its holdings in Applied Radiation will continue to be 25% (fully diluted), according to the final value. The Company was granted an option to invest at similar terms, in the event that the final value of Applied Radiation will be \$30 million. The transaction is subject to obtaining the necessary authorizations, including the approval of the shareholder meetings of the Company and Elron.

The accounting treatment of the outcome of the transaction will be made according to Securities Regulations (Presentation of Transactions Between a Company and a Controlling Shareholder in the Financial Statements) – 1996.

5.8 During the period between June 30th 2004 and until the date the financial statements were approved, the Company invested NIS 5 million – directly and indirectly – primarily in venture capital.

6. Qualitative Report Regarding the Exposure to Market Risks and the Management Thereof

The following report refers to the Company and those of its wholly-owned subsidiaries, whose exposure to market risks is managed by the Company (hereinafter: “**The Corporation**”). Regarding newly-consolidated companies, see Section 6.2, below:

No material changes were recorded during the reported period in terms of the Company's exposure to market risks and the management thereof (pursuant to the instructions of the Securities Authority), as regards the Company's report in this matter, dated March 20, 2003.

6.1 Report of Linkage Bases - Consolidated

<u>As at June 30th 2004</u>	CPI-linked	Linked to the US\$	Linked to other foreign currency	Unlinked	Non-monetary balances	Total
Current Assets	41	368	116	900	781	2,206
Non-current assets	17	37	-	-	3,588	3,642
Current Liabilities	(227)	(192)	(149)	(732)	(7)	(1,307)
Non-current liabilities	(1,610)	(25)	(12)	(59)	(817)	(2,523)
Net balance sheet amounts	<u>(1,779)</u>	<u>188</u>	<u>(45)</u>	<u>109</u>	<u>3,545</u>	<u>2,018</u>

6.2 **Newly-Consolidated Companies**

No material changes were recorded during the reported period at the companies Neshet, Polgat, Kitan and Taavura in terms of the exposure to market risks and the management thereof (pursuant to the instructions of the Securities Authority). In relation to the report on this matter dated March 20, 2003.

6.3 **Positions in Derivatives**

Highly Material Changes During the Reported Period as Compared with the Annual Report

The Company has no positions in US\$/NIS options as at June 30th.

During the reported period, Taavura (a proportionately-consolidated subsidiary – 50%) conducted NIS/CPI forward transactions at a nominal sum of NIS 120 million per annum. These transactions were intended to hedge CPI-linked loans and are recognized for accounting purposes so that in the event that the CPI rises above 1%, Taavura will receive the difference, while if the opposite occurs, it will pay the difference. The fair value of these contracts as at the date of the report is smaller than NIS 1 million.

6.4 **Events Subsequent to the Balance Sheet Date**

No material events were recorded in respect of market risks subsequent to the balance sheet date.

7. **Share Capital**

During the reported period, 150,874 shares were issued on account of the exercise of 687,080 options from the Company's stock option plans.

We wish to thank the Group's employees and managers for their contribution to the advancement and development of the Group.

Clal Industries and Investments Ltd.

Summarized Consolidated Interim Financial Statements

As at June 30th 2004
(Unaudited)

Clal Industries and Investments Ltd.

**Summarized Consolidated
Interim Financial Statements
As at June 30th 2004**

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Clal Industries & Investment Ltd.

Consolidated Balance Sheets

	June 30 th		December 31 st
	2004	2003	2003
	(Unaudited)		(Audited)
	NIS millions		
	Reported ⁽¹⁾	Adjusted ⁽²⁾	
<u>Current Assets</u>			
Cash and cash equivalents	622	111	250
Short-Term Investments	125	79	174
Accounts Receivable - Trade	525	433	451
Other Accounts Receivable	217	(*)110	(*)141
Inventories	717	665	613
	2,206	1,398	1,629
 <u>Long-Term Deposits, Loans and Receivables</u>	16	35	12
 <u>Investments</u>			
In associated companies	1,053	(*)1,225	(*)1,262
Other	353	(*)374	(*)382
	1,406	1,599	1,644
 <u>Fixed Assets</u>			
Cost	7,210	5,652	5,707
Less - accumulated depreciation	5,203	3,958	4,044
	2,007	1,694	1,663
 <u>Other Assets and Deferred Charges</u>	213	(*) 217	224
	5,848	4,943	5,172

	June 30 th		December 31 st
	2004	2003	2003
	(Unaudited)		(Audited)
NIS millions			
	Reported ⁽¹⁾	Adjusted ⁽²⁾	
<u>Current Liabilities</u>			
Credit from Banks	531	813	808
Trade Payables	331	261	303
Other accounts payable	423	350	368
Other Current Liabilities	22	142	36
	<u>1,307</u>	<u>1,566</u>	<u>1,515</u>
<u>Long-Term Liabilities</u>			
Debentures	1,484	466	905
Loans	207	237	252
Deferred Taxes	295	(*)236	(*)235
Accrued Post-Retirement/Post-Employment Benefits	165	111	133
Other liabilities	29	30	29
	<u>2,180</u>	<u>1,080</u>	<u>1,554</u>
<u>Minority Interests</u>	<u>343</u>	<u>100</u>	<u>95</u>
<u>Shareholders' Equity</u>	<u>2,018</u>	<u>2,197</u>	<u>2,008</u>
	<u>5,848</u>	<u>4,943</u>	<u>5,172</u>

(*) Reclassified.

⁽¹⁾ See Note 2.

⁽²⁾ Adjusted to the NIS of December 2003.

Date of approval of the financial statements:
August 19, 2004

Clal Industries & Investment Ltd.

Consolidated Statements of Income

	For the six-month period ended		For the three-month period ended		For the year ended
	June 30 th		June 30 th		December 31 st
	2004	2003	2004	2003	2003
	(Unaudited)		(Unaudited)		(Audited)
NIS millions					
	Reported ⁽¹⁾	Adjusted ⁽²⁾	Reported ⁽¹⁾	Adjusted ⁽²⁾	Adjusted ⁽²⁾
Revenues, net					
Sales and services	1,552	1,258	849	635	2,702
Group's equity in earnings (losses) of associated companies	30	(*) (72)	(12)	(*) (40)	(*) (21)
Other income	252	-	116	-	-
	<u>1,834</u>	<u>1,186</u>	<u>953</u>	<u>595</u>	<u>2,681</u>
Costs and expenses					
Cost of Sales and Services	1,083	900	579	433	1,908
Selling and Marketing Expenses	223	201	114	99	419
General & Administrative Expenses	103	104	56	60	196
Other expenses, net	-	(*) 103	-	(*) 67	(*) 154
Financial Expenses, net	60	62	42	44	117
	<u>1,469</u>	<u>1,370</u>	<u>791</u>	<u>703</u>	<u>2,794</u>
Income (loss) before taxes on income	365	(184)	162	(108)	(113)
Taxes on Income	76	13	44	13	10
Income (loss) after taxes on income	289	(197)	118	(121)	(123)
Minority interest in subsidiary earnings, net	33	9	30	2	6
Net Income (loss)	<u>256</u>	<u>(206)</u>	<u>88</u>	<u>(123)</u>	<u>(129)</u>
Net Income (Loss) per NIS 1 Par Value of Share Capital (In NIS)	<u>1.63</u>	<u>(1.31)</u>	<u>0.56</u>	<u>(0.79)</u>	<u>(0.82)</u>

(*) Reclassified.

(1) See Note 2.

(2) Adjusted to the NIS of December 2003.

The notes to the financial statements constitute an integral part thereof.

Clal Industries & Investment Ltd.

Statements of Changes in Shareholders' Equity

	Share Capital	Capital Reserves (*)	Retained Earnings		Total
			Dividend declared subsequent to balance sheet date	Undistributed retained earnings	
Unaudited - Reported NIS Millions ⁽¹⁾					
Balance as at January 1, 2004 (audited)	1,257	339	270	142	2,008
Issue of share capital	**	-	-	-	**
Dividend	-	-	(270)	-	(270)
Differences arising from financial statements of investee companies adjusted to foreign currency	-	24	-	-	24
Net Income	-	-	-	256	256
Dividend declared subsequent to balance sheet date	-	-	250	(250)	-
Balance as at June 30 th 2004	<u>1,257</u>	<u>363</u>	<u>250</u>	<u>148</u>	<u>2,018</u>
Unaudited - Adjusted NIS Millions ⁽²⁾					
Balance as at January 1, 2003 (audited)	1,257	403	-	847	2,507
Differences arising from financial statements of investee companies adjusted to foreign currency	-	(104)	-	-	(104)
Loss	-	-	-	(206)	(206)
Balance as at June 30 th 2003	<u>1,257</u>	<u>299</u>	<u>-</u>	<u>641</u>	<u>2,197</u>
Unaudited - Reported NIS Millions ⁽¹⁾					
Balance as at April 1, 2004	1,257	371	-	310	1,938
Issue of share capital	**	-	-	-	**
Differences arising from financial statements of investee companies adjusted to foreign currency	-	(8)	-	-	(8)
Net Income	-	-	-	88	88
Dividend declared subsequent to balance sheet date	-	-	250	(250)	-
Balance as at June 30 th 2004	<u>1,257</u>	<u>363</u>	<u>250</u>	<u>148</u>	<u>2,018</u>
Unaudited - Adjusted NIS Millions ⁽²⁾					
Balance as at April 1, 2003	1,257	383	-	764	2,404
Differences arising from financial statements of investee companies adjusted to foreign currency	-	(84)	-	-	(84)
Loss	-	-	-	(123)	(123)
Balance as at June 30 th 2003	<u>1,257</u>	<u>299</u>	<u>-</u>	<u>641</u>	<u>2,197</u>
Audited - Adjusted NIS Millions ⁽²⁾					
Balance as at January 1, 2003	1,257	403	-	847	2,507
Differences arising from financial statements of investee companies adjusted to foreign currency	-	(64)	-	-	(64)
Dividend	-	-	-	(306)	(306)
Loss	-	-	-	(129)	(129)
Dividend declared subsequent to balance sheet date	-	-	270	(270)	-
Balance as at December 31, 2003	<u>1,257</u>	<u>339</u>	<u>270</u>	<u>142</u>	<u>2,008</u>

The notes to the financial statements constitute an integral part thereof.

Clal Industries & Investment Ltd.

Statements of Changes in Shareholders' Equity (Cont'd)

(*) **Composition:**

	June 30 th		December 31 st
	2004	2003	2003
	(Unaudited)		(Audited)
	NIS millions		
	Reported ⁽¹⁾	Adjusted ⁽²⁾	
Capital Reserves			
Premium on shares	574	574	574
Capitalized earnings	23	23	23
Expired warrants of investee companies	12	12	12
Erosion of capital note issued to a company in the IDB Group	5	5	5
	<u>614</u>	<u>614</u>	<u>614</u>
Differences arising from financial statements of investee companies adjusted to foreign currency			
	(251)	(315)	(275)
	<u>363</u>	<u>299</u>	<u>339</u>

**** Sum smaller than NIS 1 million.**

⁽¹⁾ See Note 2.

⁽²⁾ Adjusted to the NIS of December 2003.

The notes to the financial statements constitute an integral part thereof.

Clal Industries & Investment Ltd.

Consolidated Statements of Cash Flows

	For the six-month period ended June 30 th		For the three-month period ended June 30 th		For the year ended December 31 st
	2004	2003	2004	2003	2003
	(Unaudited)		(Unaudited)		(Audited)
	NIS millions				
	Reported ⁽¹⁾	Adjusted ⁽²⁾	Reported ⁽¹⁾	Adjusted ⁽²⁾	Adjusted ⁽²⁾
<u>Cash Flows from Operating Activities</u>					
Net Income (loss)	256	(206)	88	(123)	(129)
Adjustments required to reflect cash flows from operating activities (a)	(133)	287	(29)	176	459
Net cash provided by operating activities	123	81	59	53	330
<u>Cash Flows from Investing Activities</u>					
Acquisition of fixed and other assets	(35)	(33)	(17)	(17)	(72)
Acquisition of newly-consolidated subsidiaries (b)	12	-	-	-	6
Investments in associated and other companies	(29)	(60)	(14)	(22)	(99)
Decrease in marketable securities, net	-	1	-	(2)	3
Proceeds from sale of fixed and other assets	9	5	5	1	13
Proceeds from realization of investments	480	72	220	-	88
Proceeds from sale of company proportionately-consolidated in the past (c)	-	-	-	-	-
Decrease (increase) in short-term deposits and loans, net	(25)	37	(11)	7	(24)
Short-term investments in IDB Group companies, net	59	-	105	-	(28)
Increase in deposits and long-term loans	(2)	(2)	(2)	(2)	(8)
Collection of long-term loans and other receivables	24	22	-	18	40
Net cash provided by (used in) investing activities	493	42	286	(17)	(81)
<u>Cash Flows from Financing Activities</u>					
Receipt of loans and other long-term liabilities:					
Banks and others	89	56	47	22	99
Issue of debentures	540	-	428	-	440
Repayment of loans and other long-term liabilities:					
Banks and others	(106)	(226)	(54)	(137)	(352)
Companies in the IDB Group	(5)	(5)	-	-	(5)
Redemption of debentures	-	-	-	-	(10)
Short-term credit from banks, net	(463)	25	(384)	14	101
Increase (decrease) in other current liabilities, net	(31)	87	-	37	(10)
Issue of shares to minority interest in consolidated subsidiary	1	-	1	-	-
Dividend paid to minority interest in subsidiaries	-	(7)	-	(7)	(14)
Dividend distributed	(270)	-	(270)	-	(306)
Net cash used in financing activities	(245)	(70)	(232)	(71)	(57)
<u>Translation Differences in Respect of Cash Balances Held by Autonomous Investee Companies</u>					
	1	(1)	(1)	(1)	(1)
Increase (Decrease) in Cash and Cash Equivalents	372	52	112	(36)	191
Cash and Cash Equivalents at Beginning of Period	250	59	510	147	59
Cash and Cash Equivalents at End of Period	622	111	622	111	250

The notes to the financial statements constitute an integral part thereof.

Clal Industries & Investment Ltd.

Consolidated Statements of Cash Flows (Cont'd)

	For the six-month period ended June 30 th		For the three-month period ended June 30 th		For the year ended December 31 st
	2004	2003	2004	2003	2003
	(Unaudited)		(Unaudited)		(Audited)
	NIS millions				
	Reported ⁽¹⁾	Adjusted ⁽²⁾	Reported ⁽¹⁾	Adjusted ⁽²⁾	Adjusted ⁽²⁾
(a) Adjustments required to reflect cash flows from operating activities					
Revenues and expenditures not affecting cash flows:					
Minority interest in subsidiary earnings, net	33	9	30	2	6
Equity in losses (earnings) of associated companies, net (*)	(11)	87	12	41	63
Losses (gains) from realization of investments, net	(266)	16	(126)	15	14
Impairment of other investments and assets	26	71	15	54	88
Depreciation and Amortization	92	86	50	42	171
Gain from realization of fixed and other assets, net	(5)	(2)	(4)	(1)	(4)
Deferred taxes, net	28	(13)	8	(1)	(48)
Increase (decrease) in accrued post-retirement/post-employment benefits	(5)	13	(2)	6	34
Erosion of assets and liabilities, net	14	1	16	6	-
Changes in asset and liability items:					
Decrease (increase) in receivables and prepayments	(23)	(3)	(22)	(17)	9
Decrease (increase) in inventories	(9)	13	13	16	70
Increase (decrease) in payables	(7)	9	(19)	13	56
	<u>(133)</u>	<u>287</u>	<u>(29)</u>	<u>176</u>	<u>459</u>
(*) Dividends received	<u>19</u>	<u>15</u>	<u>-</u>	<u>1</u>	<u>42</u>

(b) Acquisition of newly-consolidated companies (including transition from proportionate to full consolidation):

Assets and liabilities of subsidiaries as at the date of acquisition:

Deficit in working capital, net of cash	35				3
Investments in investee and other companies	(12)				8
Fixed assets, other assets and deferred charges	(398)				(13)
Long-Term Liabilities	176				7
Minority Interests	211				1
	<u>12</u>				<u>6</u>

The notes to the financial statements constitute an integral part thereof.

Clal Industries & Investment Ltd.

Consolidated Statements of Cash Flows (Cont'd)

For the six-month period ended June 30 th		For the three-month period ended June 30 th		For the year ended December 31 st
2004	2003	2004	2003	2003
(Unaudited)		(Unaudited)		(Audited)
NIS millions				
Reported ⁽¹⁾	Adjusted ⁽²⁾	Reported ⁽¹⁾	Adjusted ⁽²⁾	Adjusted ⁽²⁾

**(c) Proceeds from sale of company
proportionately-consolidated in the past**

Assets and liabilities of subsidiaries as at
the date of sale -

Investments, fixed assets, other assets and
deferred charges

Long-Term Liabilities

Capital gain on sale of investment

2	2	2
(1)	(1)	(1)
(1)	(1)	(1)
-	-	-

(d) Non-Cash Operations

Sale of fixed assets on credit

Acquisition of fixed assets on credit

Transfer of inventories to fixed assets

Repayment of liability to invest in
companies

2			
	2		7
5		3	2
	12		

⁽¹⁾ See Note 2.

⁽²⁾ Adjusted to the NIS of December 2003.

Clal Industries & Investment Ltd.

Notes to the Financial Statements
(Unaudited)

Note 1: General

- A. These financial statements are formulated in a summarized format as at June 30, 2004 and for the three-month and six-month periods then ended, in accordance with generally-accepted accounting principles pertaining to financial statements for interim periods. These financial statements should be perused within the context of the Company's annual financial statements as at December 31, 2003 and for the year then ended, including the accompanying notes.
- B. The Company is a subsidiary of IDB Development Corporation Ltd. The term "IDB Group company" in these financial statements refers to an investee company of the parent company, except companies in the Clal Industries and Investments Ltd. Group itself ("investee companies"). The term "Group companies" in these financial statements refers to the Company and its investee companies.

Note 2: Significant Accounting Policies

- A. The interim financial statements are formulated in accordance with generally-accepted accounting principles for the preparation of financial statements for interim periods, as stipulated in Accounting Standard No. 14 of the Israeli Accounting Standards Board (hereinafter: "The Standards Board"). The significant accounting policies and calculation methods that were implemented in the formulation of the interim financial statements are identical to those that were implemented in the formulation of the last annual financial statements, except for the following.
- B. Discontinuation of the adjustment of financial statements and financial reporting in reported sums

In 2001, the Standards Board issued Accounting Standard No. 12, pertaining to the "Discontinuation of Adjustment of Financial Statements". Pursuant to this standard (and its amendment in Accounting Standard No. 17), the adjustment of financial statements to inflation is to be discontinued as of January 1, 2004. The Company has implemented the directives of the standard and such adjustment was discontinued as of January 1, 2004.

Clal Industries & Investment Ltd.

Notes to the Financial Statements

(Unaudited)

1. Point of Reference for the Formulation of Financial Statements

- (a) In the past, the Company formulated its financial statements on the basis of the historical cost convention, adjusted for changes in the general purchasing power of the Israeli currency, on the basis of changes in the Consumer Price Index (CPI). The said adjusted amounts, included in the financial statements as at December 31, 2003 (the transition date), served as the reference point for the nominal financial reporting as of January 1, 2004. Any supplements made during the period were included at their nominal value.
- (b) The amounts of non-monetary assets do not necessarily reflect the realization value or current economic value, but only the reported value of those assets.
- (c) The term “cost” in these financial statements signifies cost in the reported amount.
- (d) All the comparison figures for preceding periods are presented adjusted to the CPI of the Transition Date (CPI of December 2003).

Clal Industries & Investment Ltd.

Notes to the Financial Statements (Cont'd)
(Unaudited)

Note 2: Significant Accounting Policies (Cont'd)

2. Financial Statements in Reported Amounts

(a) Definitions

Adjusted Amount – An historical nominal amount, adjusted to the CPI of December 2003, in accordance with the directives of Opinions 23 and 36 of the Institute of Certified Public Accountants in Israel.

Reported Sum – An amount adjusted to the Transition Date, with the addition of amounts in nominal values that were added subsequent to the Transition Date, net of sums deducted subsequent to the Transition Date. The deduction of sums subsequent to the Transition Date is made in nominal values, in amounts adjusted to the Transition Date or in a combination of nominal values and amounts adjusted to the Transition Date, as the case may be.

(b) Balance Sheets

- 1) Non-monetary items are presented in Reported Sums.
- 2) Monetary items are presented in the balance sheets in nominal values as at the balance sheet date.
- 3) The equity value of investments in associated companies is determined on the basis of the financial statements in Reported Sums of these companies.

(c) Statement of Income

- 1) Revenues and expenditures originating from non-monetary items or from provisions included in the balance sheets, are derived from the changes between the Reported Sum in the opening balance and the Reported Sum in the closing balance.
- 2) The remaining components of the statement of income are presented in nominal values.

Clal Industries & Investment Ltd.

Notes to the Financial Statements (Cont'd)

(Unaudited)

3) The Company's share in the operating results of associated companies is determined on the basis of the financial statements of these companies, in Reported Sums.

(d) Statements of Changes in Shareholders' Equity

Dividend declared during the reported period is presented in nominal values.

(e) The following are data pertaining to the Consumer Price Index and the exchange rate of the US dollar:

	Consumer Price Index <u>Points</u>	Exchange Rate of US\$ 1 <u>NIS</u>
<u>As at</u>		
June 30, 2004	107.7	4.497
June 30, 2003	107.7	4.312
December 31, 2003	106.2	4.379
<u>Rate of change during period</u>	<u>%</u>	<u>%</u>
Six months ended on:		
June 30, 2004	1.4	2.7
June 30, 2003	(0.5)	(9.0)
Three months ended on:		
June 30, 2004	1.5	(0.7)
June 30, 2003	(1.3)	(8.0)
Year ended December 31, 2003	(1.9)	(7.6)

3. Financial statements of autonomous investee units adjusted to foreign currency

Accounting Standard No. 13, setting rules regarding the effects of changes in foreign exchange rates, entered into effect on January 1, 2004 (hereinafter: "Standard 13"). Standard 13 replaces the directives of Clarifications No. 8 and 9 to Opinion 36 of the Institute of CPAs in Israel, which become null and void upon the entering into effect of Accounting Standard 12, as described above.

Clal Industries & Investment Ltd.

Notes to the Financial Statements (Cont'd)

(Unaudited)

Standard 13 establishes the accounting treatment for foreign currency transactions and for the translation of the financial statements of autonomous investee units (hereinafter: "The Units"), for the purpose of integrating them in the financial statements of the reporting corporation.

Pursuant to Standard 13, the monetary and non-monetary assets and liabilities of the units are translated according to the closing rate. The statement of income items and the statements of cash flows items of the Units are translated according to the exchange rate on the date of the transactions, or according to average exchange rates during the period, when these exchange rates are similar to the actual exchange rates. All the exchange rate differentials created are allocated as a separate item in the Company's shareholders' equity ("Differences arising from financial statements of certain investees adjusted to foreign currency"), until the realization of the investment.

Pursuant to Standard 13, goodwill originating from the acquisition of the units is treated as an asset of that same unit and is translated according to the closing rate and not according to the actual rate used in the transaction, as was the practice until December 31, 2003. Furthermore, statements of income items and statements of cash flows items are no longer translated according to the closing rate, but according to the described above, while non-monetary items, such as fixed assets, are no longer adjusted to changes in the Consumer Price Index overseas, prior to translation into NIS.

Clal Industries & Investment Ltd.

Notes to the Financial Statements (Cont'd)

(Unaudited)

Note 3: Investments

A. Principal Changes During the Reported Period

- The option that was granted by the Company to CRH (Israel) Ltd. (hereinafter: "CRH"), within the framework of the agreement that was signed between the parties in August 2001, for the acquisition of an additional 25% of the share capital of Mashav Initiating and Development Ltd., held by the Company, expired on December 31, 2003 (hereinafter: "The Option"). In the course of the first quarter, the company and CRH continued to negotiate for the sale of 25% of the Mashav shares. It was agreed that during the negotiations, the rights of the parties would be maintained, according to the arrangements that were in place during the option period. At the end of March 2004, the parties agreed that the rights for joint management that existed during the option period will not be extended. Subsequent to the end of the first quarter, the Company and CRH agreed to discontinue their contacts for the sale of the additional 25% of Mashav shares.

Accordingly, in the first quarter of 2004, the Company included – by proportionate consolidation (at a rate of 75%) – the Mashav statements of income. Starting March 31, 2004, Mashav's assets and liabilities, as well as its results of operation, are fully consolidated in the Company's financial statements. The addition to the consolidated assets as at March 31st 2004 amounts to approximately NIS 463 million and the supplemental net revenues from sales and services – for the three-month and six-month periods ended June 30th 2004, amount to NIS 96 million.

- In January 2004, the Company sold its entire holdings in the shares of Ormat Industries Ltd. (hereinafter: "Ormat") in a non-stock-exchange transaction, in return for NIS 259 million. The Company recorded net income of approximately NIS 113 million as a result of this sale.

In April 2004, the Company sold its holdings in Series G convertible debentures and Series H stock options for Ormat shares, in a non-stock-exchange transaction, in return for NIS 43 million. As a result of the sale, the Company recorded net earnings of NIS 15 million.

Clal Industries & Investment Ltd.

Notes to the Financial Statements (Cont'd)

(Unaudited)

- In February 2004, the Company signed an agreement for the sale of all its holdings in Negevtech Ltd. (hereinafter: "Negevtech"), in return for a sum of NIS 65 million. Under certain conditions, derived from the cost of additional acquisitions of Negevtech shares by the buyers from the Negevtech shareholders (if any), during the 15 months beginning with the closing of the sale, the Company may potentially receive additional proceeds.
The sale was finalized in May and given the immediate proceeds alone, the Company recorded net earnings of NIS 33 million.

- In May and June 2004, the Company and a partnership under its control sold 75% of their holdings in PowerDsine Ltd. (hereinafter: "PowerDsine"), in return for an overall sum of NIS 73 million. As a result of the sale, the Company recorded net earnings of NIS 23 million.
Subsequent to the said sales, the overall holding rate of the Company and the partnership it controls in PowerDsine is equal to 2.7%.

The PowerDsine shares were registered for trade on NASDAQ as part of an IPO in June 2004. As part of the IPO, the company and the partnership it controls undertook not to sell their remaining holdings in PowerDsine shares until December 2004.

- In May 2004, the Company sold all its holdings in Opticanada Inc. in return for NIS 36 million. As a result of the sale, the Company recorded net earnings of NIS 14 million.

- In May 2004, ECI Telecom Ltd. (hereinafter: "ECI") distributed to its shareholders most of its holdings in the share capital of ECTel Ltd. (hereinafter: "ECTel"), in accordance with the value of these shares in the ECI books as at the date of the transfer. Following the said distribution, the Company holds approximately 6% of the ECTel share capital. The company undertook not to sell the said shares for a period of one year from the distribution date.

Clal Industries & Investment Ltd.

Notes to the Financial Statements (Cont'd)

(Unaudited)

- In January 2004, Scitex Corporation Ltd. (hereinafter: "Scitex") announced that it intends to distribute a sum of \$118 million to its shareholders, of which \$86 million will be in cash, while the remaining \$32 million are to be distributed by way of an independent acquisition of its own shares, through a special tender offer, pursuant to the Companies Law. On May 14th 2004, Scitex published a detailed tender offer (hereinafter: "The Tender Offer"), pursuant to which Scitex acquired approximately 5 million of its own shares in June 2004 (representing approximately 11.5% of the issued share capital and voting rights in Scitex prior to the tender offer), in return for an overall sum of \$28 million. The Company, together with Discount Investments Ltd. (hereinafter: "DIC"), a subsidiary of the Company's parent company, sold 0.26 million Scitex shares as part of the tender offer.

Subsequent to the completion of the tender offer, the Company's holding rate in Scitex is equal to 24.7%. The overall holding rate (together with DIC) totals 49.1%.

In June 2004, Scitex decided to distribute \$90 million in cash to its shareholders. This sum was distributed in July 2004. The Company's share in the distribution amounted to \$22 million. The Company's share in the said distribution is presented in the balance sheets under "Accounts Receivable".

- In June 2004, following a downturn in the business situation of Shellcase Ltd. (hereinafter: "Shellcase"), the Company analyzed its investment in Shellcase and decided to include in its accounts a write-down for the impairment of its investment and the investment of partnerships under its control in shares and in a loan convertible into shares of Shellcase, equal to the full investment in the books, in the total sum of NIS 18 million. The sum written down was allocated to the statements of income under "Group's equity in earnings (losses) of associated companies".

Clal Industries & Investment Ltd.

Notes to the Financial Statements (Cont'd)
(Unaudited)

Note 3: Investments (Cont'd):

B. Investments in Listed Companies

	Sum of investment in shares, as presented in the balance sheets as at June 30, 2004	Value on stock exchange as at	
		June 30 th 2004	August 17 th 2004
NIS millions			
Associated Companies:			
ECI Telecom Ltd.	293	467	435
American Israeli Paper Mills Ltd. Group	207	326	297
Scitex Corporation Ltd.	169	(*)163	168
Fundtech Ltd.	110	185	158
Maman - Cargo Terminals and Handling Ltd.	31	44	40
Cargal Ltd.	30	27	22
Nova Measuring Instruments Ltd.	28	50	40
Beit Shemesh Engine Holdings (1997) Ltd.	18	19	17
Gold Bond Group Ltd.	9	12	11
Other companies:			
Compugen Ltd.	23	64	46
ECTel Ltd.	14	14	12
PowerDsine Ltd.	13	26	19
Other	8	15	12

(*) Net of cash distribution of NIS 100 million.

Clal Industries & Investment Ltd.

Notes to the Financial Statements (Cont'd)
(Unaudited)

Note 4: Attached Financial Statements of Associated Companies:

The Company is attaching to these financial statements, the financial statements of associated companies ECI and Scitex. Following are the effects of the adjustment of the financial statements of the said companies, reported according to generally accepted accounting principles in the U.S., to generally accepted accounting principles in Israel:

	As at June 30 th				As at December 31	
	2004		2003		2003	
	ECI	Scitex	ECI	Scitex	ECI	Scitex
	Unaudited				Audited	
\$ thousands						
Shareholders' equity:						
As reported by the associated company	546,782	156,527	600,319	214,030	569,505	224,698
Net adjustments to generally accepted accounting principles in Israel	861	(1,798)	3,055	(6,685)	631	(7,500)
Adjusted amount	547,643	154,729	603,374	207,345	570,136	217,198

	For the six-month period ended June 30 th				For the three-month period ended June 30 th				For the year ended December 31, 2003	
	2004		2003		2004		2003		Audited	
	ECI	Scitex	ECI	Scitex	ECI	Scitex	ECI	Scitex	ECI	Scitex
	Unaudited				Unaudited				Audited	
\$ thousands										
Net income (loss) for the period:										
As reported by the associated company	(4,753)	49,053	(42,798)	(11,592)	(3,527)	(1,236)	(34,992)	(4,840)	(71,040)	1,387
Net adjustments to generally accepted accounting principles in Israel	4,936	5,702	(1,885)	(2,248)	2,141	(42)	1,911	(1,037)	(9,526)	(3,811)
Adjusted amount	183	54,755	(44,683)	(13,840)	(1,386)	(1,278)	(33,081)	(5,877)	(80,566)	(2,424)

Clal Industries & Investment Ltd.

Notes to the Financial Statements (Cont'd)
(Unaudited)

Note 5: Dividend

In March 2004, the Company's Board of Directors decided to distribute a cash dividend in the sum of NIS 270 million, representing NIS 1.72 for every NIS 1 par value of shares. The dividend distribution was made on April 28, 2004.

Regarding dividends announced subsequent to the balance sheet date, see Note 11b, below.

Note 6: Data Regarding Business Sectors

	For the six-month period ended		For the three-month period ended		For the year ended
	June 30 th		June 30 th		December 31 st
	2004	2003	2004	2003	2003
	(Unaudited)		(Unaudited)		(Audited)
NIS millions					
	Reported ⁽¹⁾	Adjusted ⁽²⁾	Reported ⁽¹⁾	Adjusted ⁽²⁾	Reported ⁽¹⁾
A. Sector revenues ⁽³⁾					
Cement	473	365	285	208	808
Textile	827	721	413	351	1,547
High-technology and electronics	57	(46)	(3)	(23)	12
Venture Capital Funds	(9)	(4)	(5)	(1)	(9)
Biotechnology	(12)	(30)	(2)	(17)	(36)
Real Estate	58	33	39	6	49
Others	188	147	110	71	310
	<u>1,582</u>	<u>1,186</u>	<u>837</u>	<u>595</u>	<u>2,681</u>
Other income, net *	252	-	116	-	-
Total in statements of income	<u>1,834</u>	<u>1,186</u>	<u>953</u>	<u>595</u>	<u>2,681</u>
* Cement	6		1		
Textile	(3)		(5)		
High-technology and electronics	52		55		
Venture Capital Funds	20		21		
Biotechnology	(9)		(1)		
Real Estate	(2)		(3)		
Others	188		48		
	<u>252</u>		<u>116</u>		

⁽¹⁾ See Note 2.

⁽²⁾ Adjusted to the NIS of December 2003.

⁽³⁾ Including sector's share in losses of associated companies

Note 6: Data Regarding Business Sectors (Cont'd)

Clal Industries & Investment Ltd.

Notes to the Financial Statements (Cont'd)
(Unaudited)

	For the six-month period ended		For the three-month period ended		For the year ended
	June 30 th		June 30 th		December 31 st
	2004	2003	2004	2003	2003
	(Unaudited)		(Unaudited)		(Audited)
	NIS millions				
	Reported ⁽¹⁾	Adjusted ⁽²⁾	Reported ⁽¹⁾	Adjusted ⁽²⁾	Reported ⁽¹⁾
B. Sector Results					
Cement	117	28	83	50	119
Textile	25	18	7	16	36
High-technology and electronics	84	(103)	39	(67)	(73)
Venture Capital Funds	10	(24)	16	(8)	(30)
Biotechnology	(36)	(57)	(11)	(35)	(93)
Real Estate	21	17	15	(5)	27
Others	⁽⁴⁾ 206	12	⁽⁴⁾ 59	1	38
	<u>427</u>	<u>(109)</u>	<u>208</u>	<u>(48)</u>	<u>24</u>
Adjustments ⁽³⁾	(2)	(13)	(4)	(16)	(20)
Financial Expenses	<u>(60)</u>	<u>(62)</u>	<u>(42)</u>	<u>(44)</u>	<u>(117)</u>
Income (loss) before taxes on income	<u><u>365</u></u>	<u><u>(184)</u></u>	<u><u>162</u></u>	<u><u>(108)</u></u>	<u><u>(113)</u></u>

⁽¹⁾ See Note 2.

⁽²⁾ Adjusted to the NIS of December 2003.

⁽³⁾ Including other expenses, net, not allocated to sector

⁽⁴⁾ Regarding the sale of holdings in Ormat shares and bonds – See Note 3A.

Note 7: Debentures

In June 2004, Mashav issued – by private placement – non-marketable debentures in the amount of NIS 430 million, to institutional investors (of which NIS 95 million to a related party). The debentures are linked to the CPI and bear interest at the rate of 5.4% per annum. The principal of the debentures is scheduled for repayment in nine equal annual installments, starting June 2006. As part of the offering, Mashav undertook toward the investors to refrain from creating liens in favor of other parties.

Note 8: Taxes on Income (tax benefit)

A) On June 29, 2004, the Israeli Knesset ratified an amendment to the Income Tax Ordinance (No. 140 and temporary order) – 2004 – stipulating the gradual lowering of corporate tax rates in Israel, starting January 1, 2004, from 36% to 35% in 2004 and down to 30% in 2007. The said amendment led to a decrease of NIS 42 million in the income tax expenses in the second quarter of 2004.

Clal Industries & Investment Ltd.

Notes to the Financial Statements (Cont'd)

(Unaudited)

- B. In the second quarter, a consolidated subsidiary modified its policy regarding dividend distribution from a wholly-owned subsidiary, originating from an Approved Enterprise eligible for lower tax rates. In accordance with the above, the consolidated subsidiary expects that there exists a high probability for the distribution of dividends from retained earnings in 2002 and 2003 from the Approved Enterprise and has therefore recorded deferred tax expenses in the amount of NIS 12 million.

Note 9: Impact of a New Accounting Standard in the Period Prior to its Implementation

Accounting Standard No. 19, dealing with taxes on income (hereinafter: "The Standard"), was approved in July 2004 by the Standards Board. The standard determines the rules for the recognition, measurement, presentation and disclosure pertaining to taxes on income in financial statements.

The major change outlined in the standard regarding the rules that are currently implemented at the Group concerns the recognition of deferred taxes on account of temporary differences related to land.

The new Standard will apply to financial statements covering periods beginning on or after January 1, 2005. The implementation of the standard will be made by way of the cumulative impact as at the beginning date of the period during which the standard is adopted.

The Group and the Group companies are examining the consequences of implementing the directives of the said standard, although at this stage it is impossible to estimate the impact of the standard on their financial statements.

Note 10: Financial Parameters

Within the framework of an agreement with one of the banks regarding the extension of the repayment period on a \$10 million loan received by the company from the same bank, the company undertook to meet financial parameters relating to the total of certain assets in relation to the net debt and the total of certain assets in relation to principal and interest payments in the following 12 months.

Clal Industries & Investment Ltd.

Notes to the Financial Statements (Cont'd)

(Unaudited)

Note 11: Events Subsequent to the Balance Sheet Date

- A) In August 2004, Elron Electronic Industries Ltd. (hereinafter: "Elron") (a company in which DIC holds 46%) and Applied Radiation Jordan Valley Ltd. (hereinafter: "Applied Radiation"), a subsidiary of the Company (in which the Company holds 57%), signed an investment agreement in Applied Radiation. Pursuant to the investment agreement, Elron will invest a sum of \$6.7 million in return for 25% (fully diluted) of the share capital of Applied Radiation. The said transaction is contingent upon another transaction whereby the Company will convert shareholder loans totaling \$2.25 million into share capital of Applied Radiation, at terms that are similar to the terms of the Elron investment and upon settling the terms of the outstanding loans – in the sum of \$2 million – granted by the Company to Applied Radiation. Subsequent to the Elron investment and the conversion of the said company loans, the Company's holding rate in Applied Radiation will decrease to approximately 41% (fully diluted).

The final value of Applied Radiation for the purpose of the Elron investment, subsequent to the conversion of the loans by the Company, will be determined in July 2005, according to the performance of Applied Radiation and will lie in the range between \$10 and \$30 million. The Company's and Elron's holding percentage in Applied Radiation may change accordingly. Moreover, in the event that the final value of Applied Radiation shall be higher than \$20 million, Elron will be eligible to acquire additional shares, to ensure that its holdings in Applied Radiation will continue to be 25% (fully diluted), according to the final value. The Company was granted an option to invest at similar terms, in the event that the final value of Applied Radiation will be \$30 million. The transaction is subject to obtaining the necessary authorizations, including the approval of the shareholder meetings of the Company and Elron.

The accounting treatment of the outcome of the transaction will be made according to Securities Regulations (Presentation of Transactions Between a Company and a Controlling Shareholder in the Financial Statements) – 1996.

Clal Industries & Investment Ltd.

Notes to the Financial Statements (Cont'd)

(Unaudited)

- B. On August 19, 2004, the Company announced a dividend in the sum of NIS 250 million, representing NIS 1.59 per every NIS 1 par value. The dividend will be paid on September 27th 2004, with the determining date being September 12th 2004 and the X-date being September 13th 2004. The dividend is presented under a separate item in shareholders' equity: "Dividend Declared Subsequent to Balance Sheet Date".

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