Chapter B of the Periodic Report

Directors' Report on the State of the Company's Affairs For the nine-month period ended September 30, 2008

We respectfully present the Directors' Report on the state of affairs of Bezeq - The Israel Telecommunication Corp. Limited (hereinafter: "the Company") and the consolidated Group companies (the Company and the consolidated companies together are hereinafter collectively referred to as “the Group”), for the nine month period ended September 30, 2008 (hereinafter: "the Directors' Report").

The Directors’ Report includes a condensed review of the Company’s affairs and it assumes that the Directors’ Report for December 31, 2007 is also available to the reader.

The Group operates in four main areas which are reported as business segments in the Company's consolidated reports as follows:

1. **Domestic fixed-line communications**
2. **Cellular**
3. **International communications, internet services and NEP**
4. **Multi-channel television**

The Company has an additional area of operations which is not material to the Group's operations, and which has been included in the financial statements of September 30, 2008 as another business segment, which mainly includes customer call center services and investment in a venture capital fund.

Net earnings in the first nine months of 2008 amounted to NIS 1.229 billion, compared to net earnings of NIS 1.056 billion in the corresponding period last year. Net earnings attributable to the shareholders of the Company amounted to NIS 1.329 billion, compared to NIS 1.015 billion in the corresponding period last year. The increase in net earnings is due to an increase in earnings in all segments, with the exception of the multi-channel television segment, where there was an increase in the loss. See below for further details.

1. Financial position

A. The financial statements are drafted in accordance with International Financial Reporting Standards (IFRSs).

B. The Group's assets on September 30, 2008 amounted to approximately NIS 14.74 billion, compared to approximately NIS 15.55 billion on September 30, 2007. Of these, approximately NIS 5.96 billion (40%) are property, plant and equipment, compared to approximately NIS 6.08 billion (39%) on September 30, 2007.

The decrease in the Group's assets is due to the domestic fixed-line communications segment. There was a decline in total assets in this segment, not including investment in subsidiaries, compared to the corresponding period , in the amount of NIS 1.12 billion, mainly due to the sale of financial assets held for trading, which were used for financing and investment activities. In addition, there was a decrease in the net book value of property, plant and equipment resulting from the difference between the depreciation expense and investment made during the reporting period and a decrease in the deferred taxes balance. The decrease in the assets was offset by an increase in cash and cash equivalents and in trade receivables.

In the cellular segment, assets increased from approximately NIS 4.25 billion on September 30, 2007 to approximately NIS 4.54 billion on September 30, 2008. The increase was mainly due to an increase in frequency rights and the trade receivables balance, mainly due to the termination of discounting of credit card payments. In addition, there was an increase in depreciated cost of property, plant and equipment resulting from the difference between the depreciation expense and investment made during the reporting period. On the other hand, there was a decrease in the cash balance and a reduction in the tax asset due to the sale of the asset recorded in the past for losses.

In the international communications, internet and NEP services segment, there was an increase in total assets compared to September 30, 2007, mainly due to the increase in the trade receivables balance and advance long-term expenses for user rights of capacities. The increase was offset by a reduction in the cash balances used for early payment of loans.

In the multi-channel television segment, there was an increase in total assets compared to September 30, 2007, which was mainly due to an increase in broadcasting rights and an increase in the net investment balance in property, plant and equipment.

C. The equity attributable to the shareholders of the Company on September 30, 2008, amounted to approximately NIS 4.4 billion, representing 29.9% of the total balance sheet, compared to approximately NIS 4.22 billion on September 30, 2007, representing 27% of the total balance sheet. The increase in equity is mainly due to the Group's net profit, which was mainly offset by distribution of a dividend amounting to approximately NIS 1.514 billion.

D. Group debt to financial institutions and debenture holders on September 30, 2008, amounted to approximately NIS 6.22 billion, compared to approximately NIS 6.87 billion on September 30, 2007. The decrease is mainly due to repayment of debentures in the amount of approximately NIS 601 million in the domestic fixed line communication segment. Total repayment of debentures and loans in the Group amounted to approximately NIS 922 million. The decrease was mainly offset by revaluation of the CPI-linked loans and debentures due to a sharp rise in the CPI.

The Company's auditors have highlighted the financial position of DBS in the financial statements. As mentioned in Note 5, as of September 30, 2008 DBS meets the financial criteria set for it, following the amended stipulations in respect of 2008 placed upon it by the banks on March 5, 2008 and June 25, 2008 as adapted to the subsidiary's 2008 annual budget and to certain prescribed operational data. The continuation of the operations of DBS is also conditional on compliance with conditions set for 2008 and/or further relief to be received during the year. The management of DBS believes that the financial resources available to it will be sufficient for its operational requirements in the coming year based on the forecasted cash flow approved by the board of directors of DBS.

E. The Group's cash and other current investment balances on September 30, 2008, amounted to approximately NIS 1.259 billion compared to approximately NIS 2.085 billion on September 30, 2007. The decrease is mainly due to a decrease in current investment balances in the domestic fixed-line communications segment, which was partially offset by the increase in cash balances, due to positive cash flows from current operations in this segment and in the principal segments of the Group's operations.

2. Results of operations

A. Principal results

	Nine months ended September 30				Three months ended September 30			
	2008	2007			2008	2007		
	NIS millions	NIS millions	Increase (Decrease)	%	NIS millions	NIS millions	Increase (Decrease)	%
Revenues from sales	9,345	9,280	65	0. 7%	3,159	3,139	20	0. 6%
Costs and expenses	7,059	7,457	(398)	(5.3%)	2,337	2,543	(206)	(8.1%)
Operating income	2,286	1,823	463	25.4%	822	596	226	37.9%
Financing expenses, net	469	265	204	77%	186	134	52	38.8%
Profit after financing expenses, net	**1,817**	**1,558**	**259**	**16.6%**	**636**	**462**	**174**	**37.7%**
Company's share in profits of investees accounted by the equity method	4	2	2	100%	2	1	1	100%
Profit before taxes	**1,821**	**1,560**	**261**	**16.7%**	**638**	**463**	**175**	**37.8**%
Income tax	592	504	88	17.5%	207	133	74	**55.6%**
Profit for the period	**1,229**	**1,056**	**173**	**16.4%**	**431**	**330**	**101**	**30.6%**
Attributable to:								
The shareholders of the Company	1,329	1,015	314	30.9%	462	255	207	81.2%
Non-controlling interests	(100)	41	(141)		(31)	75	(106)	
Profit for the period	**1,229**	**1,056**	**173**	**16.4%**	**431**	**330**	**101**	**30.6%**
Earnings per share								
Basic earnings per share (in NIS)	0.51	0.39	0.12	30.8%	0.18	0.10	0.08	80%
Diluted earnings per share (in NIS)	0.50	0.38	0.12	31.6%	0.17	0.09	0.08	88.9%

Group revenue in the first nine months of 2008 amounted to approximately NIS 9.35 billion compared to approximately NIS 9.28 billion in the corresponding period, an increase of approximately 0.7%.

Group revenue in the third quarter of 2008 amounted to approximately NIS 3.16 billion compared to approximately NIS 3.14 billion in the corresponding period, an increase of approximately 0.64%.

The increase is mainly due to the cellular and multi-channel television segment, which was partially offset by a decrease in the domestic fixed-line communications segment.

The Group's depreciation and amortization expenses in the first nine months of 2008 amounted to approximately NIS 1.274 billion, compared to approximately NIS 1.323 billion in the corresponding period, a decrease of approximately 3.7%.

The Group's depreciation and amortization expenses in the third quarter of 2008 amounted to approximately NIS 423 million, compared to approximately NIS 445 million in the corresponding period , a decrease of approximately 4.9%. The decrease was mainly due to the domestic fixed-line communications segment and the multichannel television segment, which was partially offset by an increase in expenses in the cellular segment.

The Group's salary expenses in the first nine months of 2008 amounted to approximately NIS 1.774 billion, compared to approximately NIS 1.757 billion in the corresponding period, an increase of approximately 1%. The increase is due to an increase in salary expenses in all segments, with the exception of the domestic fixed-line communication segment, where there was a decrease in salary expenses.

The Group's salary expenses in the third quarter of 2008 amounted to approximately NIS 573 million, compared to approximately NIS 597 million in the corresponding period, a decrease of approximately 4%. The decrease is due to a decrease in salary expenses in the domestic fixed-line communication segment, which was partially offset by an increase in salary expenses in the other Group segments.

The Group's operating and general expenses in the first nine months of 2008 amounted to approximately NIS 4.03 billion, compared to approximately NIS 4.31 billion in the corresponding period in the prior year, a decrease of approximately 6.5%.

The Group's operating and general expenses in the third quarter of 2008 amounted to approximately NIS 1.34 billion, compared to approximately NIS 1.48 billion in the corresponding period in the prior year, a decrease of approximately 9.5%. The decrease is due to a decrease in expenses in all the segments.

Profit for the period attributable to the shareholders of the Company in the first nine months of 2008 amounted to NIS 1.329 million, and in the third quarter NIS 462 million. Profit was affected by the early application of international standards, whereby 58% of the losses of DBS were included in the part of the Company's shareholders – for further details, see Note 3(A)(4) to the financial statements.

B. Operating segments

Below are details of operations according to segments stated by the operating segments of the Group:

Revenue by segment of operations	1-9/2008		1-9/2007		7-9/2007		7-9/2007	
	NIS millions	% of total revenues	NIS millions	% of total revenues	NIS millions	% of total revenues	NIS millions	% of total revenues
Domestic fixed-line communication	4,150	44.4%	4,260	45.9%	1,388	43.9%	1,425	45.4%
Cellular	3,575	38.2%	3,502	37.7%	1,214	38.4%	1,203	38.3%
International communications, internet and NEP services	969	10.4%	970	10.5%	329	10.4%	326	10.4%
Multi-channel television	1,136	12.2%	1,067	11.5%	375	11.9%	360	11.5%
Others and adjustments	(485)	(5.2%)	(519)	(5.6%)	(147)	(4.6%)	(175)	(5.6%)
Total	9,345	100%	9,280	100%	3,159	100%	3,139	100%

Operating income by segment of operations	1-9/2008		1-9/2007		7-9/2007		7-9/2007	
	NIS millions	% of total revenues	NIS millions	% of total revenues	NIS millions	% of total revenues	NIS millions	% of total revenues
Domestic fixed-line communications	1,218	29.3%	939	22.0%	422	30.4%	327	23.0%
Cellular	774	21.6%	672	19.2%	293	24.1%	219	18.2%
International communications, internet and NEP services	176	18.2%	159	16.4%	59	17.9%	54	16.6%
Multi-channel television	122	10.7%	51	4.8%	52	13.9%	(4)	(1.1%)
Other and setoffs	(4)		2		(4)		-	
Operating income	2,286		1,823		822		596	

Domestic fixed-line communications

Revenues:

Revenues in the first nine months of 2008 amounted to approximately NIS 4.15 billion compared to approximately NIS 4.26 billion in the corresponding period in the prior year, a decrease of approximately 2.6%.

Revenues from the segment in the quarter amounted to approximately NIS 1.39 billion compared to NIS 1.43 billion in the corresponding period last year, a decrease of approximately 2.8%.

The decrease in the segment's revenue is due to a decrease in interconnect fees to the cellular networks (as well as a decrease in expense). An additional decrease is due to a decrease in the number of lines (mainly due to number portability), a reduction in call traffic and a decrease in tariffs in June 2007 and June 2008. The decrease in revenues was offset mainly by ongoing growth in revenues from high-speed internet service (ADSL) due to an increase the number of subscribers and sales of household networks as well as due to an increase in income from data communication services. The Company's auditors continue to draw attention to the growing competition, changes in the communications market and the impact of regulation on the financial situation of the Group and the results of its operations

Costs and expenses:

Depreciation expenses in the first nine months of 2008 amounted to approximately NIS 643 million compared to approximately NIS 709 million in the corresponding period in the prior year, a decrease of approximately 9.3%.

Depreciation expenses in the quarter amounted to approximately NIS 214 million compared to approximately NIS 236 million in the corresponding quarter, a decrease of approximately 9.3%.

The decrease is due to full depreciation of property, plant and equipment and a decrease in investments in new property.

Salary expenses in the first nine months of 2008 amounted to approximately NIS 905 million compared to approximately NIS 964 million in the corresponding period , a decrease of approximately 6.1%.

Salary expenses in the quarter amounted to approximately NIS 289 million compared to approximately NIS 328 million in the corresponding quarter, a decrease of approximately 11.9%.

The decrease in salary expenses is due mainly to retirement of employees, partially offset by share-based payments.

Operating and general expenses in the first nine months of 2008 amounted to approximately NIS 1.398 billion compared to approximately NIS 1.576 billion in the corresponding period , a decrease of approximately 11.3%.

General and operating expenses in the quarter amounted to approximately NIS 464 million compared to approximately NIS 509 million in the corresponding quarter, a decrease of approximately 8.8%.

The decrease in general and operating expenses is mainly due to a reduction in interconnect fees to cellular operators alongside a decrease in income, update of the provision for royalties, cancellation of the provision for international suppliers and implementation of efficiency measures that resulted in a decrease in operating expenses.

Other operating revenues in the first nine months of 2008 amounted to approximately NIS 14 million, compared to expenses of approximately NIS 72 million in the corresponding period.

Other net operating revenues in the quarter amounted to approximately NIS 1 million compared to expenses of approximately NIS 25 million in the corresponding period. . This is mainly due to provisions recorded for lawsuits in the corresponding period compared to capital gain and a decrease in provisions in the reporting period.

Operating income:

The segment’s operating income in the first nine months of 2008 amounted to approximately NIS 1.218 billion compared to approximately NIS 939 million in the corresponding period, an increase of approximately 29.7%.

Operating income from the segment in the quarter amounted to approximately NIS 422 million compared to approximately NIS 327 million in the corresponding quarter, an increase of approximately 29%.

The improvement in operating income is due to the changes described in the expenses and revenues section above.

Cellular

Revenues:

Revenues from the segment in the first nine months of 2008 amounted to approximately NIS 3.58 billion compared to approximately NIS 3.5 billion in the corresponding period, an increase of approximately 2.3%.

Revenues from the segment in the quarter amounted to approximately NIS 1.21 billion compared to approximately NIS 1.2 billion in the corresponding quarter, an increase of approximately 0.8%.

The increase is mainly due to an increase in the number of subscribers, in particular 3G subscribers, which led to an increase in revenue from user fees and from content services. This was partially offset by a decrease in average revenue per user, mainly due to erosion of fees for outgoing calls and a decrease in interconnecting fees.

Costs and expenses:

Depreciation and amortization expenses in the first nine months of 2008 amounted to approximately NIS 388 million compared to approximately NIS 353 million in the corresponding period, an increase of approximately 9.9%.

Depreciation expenses in the quarter amounted to approximately NIS 129 million compared to approximately NIS 121 million in the corresponding quarter, an increase of approximately 6.6%.

Salary expenses in the first nine months of 2008 amounted to approximately NIS 486 million compared to approximately NIS 444 million in the corresponding period, an increase of approximately 9.5%.

Salary expenses in the quarter amounted to approximately NIS 157 million compared to approximately NIS 150 million in the corresponding quarter, an increase of approximately 4.6%.

The increase in salary expenses is mainly due to recognition of expenses for share-based payments and salary updates.

Operating and general expenses in the first nine months of 2008 amounted to approximately NIS 1.927 billion compared to approximately NIS 2.033 billion in the corresponding period, a decrease of approximately 5.2%.

General and operating expenses in the quarter amounted to approximately NIS 635 million compared to approximately NIS 713 million in the corresponding quarter, a decrease of approximately 11%.

The decrease is mainly due to a decrease in the amount of devices sold and upgraded and a decrease in costs of terminal equipment following a decrease in the dollar exchange rate.

Operating income:

Operating income in the segment in the first nine months of 2008 amounted to approximately NIS 774 million compared to approximately NIS 672 million in the corresponding period, an increase of approximately 15.2%.

Operating income in the segment in the quarter amounted to approximately NIS 293 million compared to approximately NIS 219 million in the corresponding quarter, an increase of approximately 33.8%.

The improvement in operating income is due to the changes described in the expenses and revenues sections above.

<u>International communications, internet services and NEP</u>

Revenues:

Group revenue in the first nine months of 2008 amounted to approximately NIS 696 million compared to approximately NIS 970 million in the corresponding period, a decrease of approximately 0.1%.

Revenues from the segment in the quarter amounted to approximately NIS 329 million compared to approximately NIS 326 million in the corresponding quarter, an increase of approximately 0.9%.

In this sector, there was a decrease in operations relating to call transfers between communication operators around the world. Conversely, there was an increase in the Company's revenues from outgoing international calls due to an increase in the volume of outgoing minutes, an increase in revenues from internet due to an increase in the number of broadband subscribers, and an increase in integration activities and communication solutions for corporate customers.

Costs and expenses:

Depreciation expenses in the first nine months of 2008 amounted to approximately NIS 60 million compared to approximately NIS 66 million in the corresponding period in the prior year, a decrease of approximately 9.1%.

Depreciation expenses in the quarter amounted to approximately NIS 20 million compared to approximately NIS 21 million in the corresponding quarter, a decrease of approximately 4.7%.

Salary expenses in the first nine months of 2008 amounted to approximately NIS 197 million compared to approximately NIS 182 million in the corresponding period, an increase of approximately 8.2%.

Salary expenses in the quarter amounted to approximately NIS 67 million compared to approximately NIS 61 million in the corresponding quarter, an increase of 9.8%.

The increase in salary expenses is mainly due to an increase in the number of employees in response to higher operational requirements and share-based payments.

Operating and general expenses in the first nine months of 2008 amounted to approximately NIS 535 million compared to approximately NIS 564 million in the corresponding period, a decrease of approximately 5.1%.

General and operating expenses in the quarter amounted to approximately NIS 183 million compared to approximately NIS 190 million in the corresponding quarter, a decrease of approximately 3.4%.

The decrease is mainly due to a reduction in operations relating to call transfers between communication operators around the world alongside a decrease in revenues.

Operating income:

Operating income in the segment in the first nine months of 2008 amounted to approximately NIS 176 million compared to approximately NIS 159 million in the corresponding period, an increase of approximately 10.7%.

Operating income from the segment in the quarter amounted to approximately NIS 59 million compared to approximately NIS 54 million in the corresponding quarter, an increase of approximately 9.3%.

The improvement in operating income is due to the changes described in the expenses and revenues sections above.

<u>Multichannel television</u>

Revenues:

Revenues in the segment in the first nine months of 2008 amounted to approximately NIS 1.136 million compared to approximately NIS 1.067 million in the corresponding period, an increase of approximately 6.4%.

Revenues from the segment in the quarter amounted to approximately NIS 375 million compared to approximately NIS 360 million in the corresponding quarter, an increase of approximately 4.2%.

The increase in revenues is mainly due to an increase in the average revenue per user (ARPU).

Costs and expenses:

Depreciation expenses in the first nine months of 2008 amounted to approximately NIS 184 million compared to approximately NIS 201 million in the corresponding period, a decrease of approximately 8.5%.

Depreciation expenses in the quarter amounted to approximately NIS 59 million compared to approximately NIS 69 million in the corresponding quarter, a decrease of approximately 14.5%.

Salary expenses in the first nine months of 2008 amounted to approximately NIS 142 million compared to approximately NIS 133 million in the corresponding period ,an increase of approximately 7%.

The increase in salary expenses is mainly due to an increase in the number of employees in response to the increase in operational requirements.

Salary expenses in the quarter amounted to approximately NIS 45 million compared to approximately NIS 46 million in the corresponding quarter, a decrease of approximately 2.2%.

Operating and general expenses in the first nine months of 2008 amounted to approximately NIS 688 million compared to approximately NIS 682 million in the corresponding period, an increase of approximately 0.8%. The increase is mainly due to an increase in content consumption expenses due to broadcasts of original productions, an increase in services and maintenance by subcontractors and an increase in car maintenance expenses, partially offset by a decrease in general expenses.

General and operating expenses in the quarter amounted to approximately NIS 218 million compared to approximately NIS 249 million in the corresponding quarter, a decrease of approximately 12.4%. The decrease is mainly due to a decrease in general expenses.

Operating income:

Operating income in the segment in the first nine months of 2008 amounted to approximately NIS 122 million compared to approximately NIS 52 million in the corresponding period, an increase of approximately 134.6%. The improvement in operating income is due mainly to the increase in revenues as noted above.

Operating income from the segment in the quarter amounted to approximately NIS 52 million compared to a loss of approximately NIS 4 million in the corresponding quarter. The increase in operating income in the quarter is mainly due to a decrease in operating expenses.

C. <u>Financing expenses, net</u>

The Group’s net financing expenses in the first nine months of 2008 amounted to approximately NIS 469 million compared to approximately NIS 265 million in the corresponding period last year, an increase of approximately 77%.

The Group's debt to financial institutions and debenture holders is primarily linked to the CPI and the financing expenses are affected by fluctuations in the index. During the reporting period there was a rise in the index to which the debt balance is linked, compared to the corresponding period , and revaluation of liabilities led to an increase in the Group's financing expenses.

Net financing expenses in the domestic fixed-line communication segment in the first nine months of 2008 amounted to approximately NIS 77 million compared to approximately NIS 164 million in the corresponding period last year, a decrease of approximately 53%. The decrease in net financing expenses compared to the corresponding period is mainly due to an increase in revenues from shareholders’ loans to DBS and a decrease in interest expenses, which were partially offset by an increase in linkage differences expenses and a decrease in interest revenues from deposits.

In the cellular segment, net financing expenses remain unchanged, mainly due to the increase in revaluation of CPI-linked liabilities expenses as a result of a rise in the CPI and an increase in forward transactions and embedded derivatives expenses following a decrease in the exchange rate. This was partially offset by capitalized credit costs for qualified assets and a decrease in net debt.

In the multi-channel television segment, net financing expenses in the first nine months of 2008 amounted to approximately NIS 369 million compared to approximately NIS 89 million in the corresponding period, an increase of approximately 314.6%. The change is mainly due to financing revenues of approximately NIS 213 million recognized in the third quarter in the prior year due to a change in the capitalization rate of shareholders' loans. In addition, the rise in the CPI led to an increase in financing expenses due to the revaluation of CPI-linked liabilities and an increase in the Company’s financial debt.

D. <u>Income tax</u>

The Group's tax expenses in the reporting period amounted to approximately NIS 592 million, representing approximately 32.5% of profit before taxes, compared to approximately NIS 504 million in the corresponding period, representing approximately 32.3% of profit before taxes. Most of the decrease in the tax expenses from profit before income taxes is due to a reduction in the tax rate and the cancellation of the Income Tax (Taxation under Conditions of Inflation) Law. The decrease was offset by the increase in the losses of DBS that are not tax deductible.

3. <u>Liquidity and sources of financing</u>

Consolidated cash flows generated by operating activities in the first nine months of 2008 amounted to approximately NIS 2.65 billion, compared to approximately NIS 2.38 billion in the corresponding period, an increase of approximately NIS 271 million. The increase in cash flows generated by operating activities is mainly due to an increase in operating income in all segments of the Group, and to a change in the balance of trade receivables, which was partially offset by a rise in payments in respect of early retirement, a change in the balance of accounts payable and a decrease in interest received.

Cash flows generated by operating activities are one of the sources of financing of the Group's investments, which during the reporting period included approximately NIS 962 million invested in development of communications infrastructures, compared to investments amounting to approximately NIS 681 million in the corresponding period.

In the reporting period, the Group repaid net debts and paid interest of approximately NIS 1.044 billion, of which approximately NIS 697 million was on account of debentures, NIS 112 million of loans, NIS 266 million of interest payments and NIS 5 million of short-term credit. On the other hand, the Company's net proceeds from the realization of derivative financial instruments was approximately NIS 36 million, compared to payment of net debt and interest payments in the amount of approximately NIS 3.001 billion in the corresponding period.

In the reporting period, cash dividends amounting to approximately NIS 679 million were paid, compared to approximately NIS 2.1 billion paid in the corresponding period.

The monthly average short-term credit average from banks in the first nine months of 2008 amounted to approximately NIS 97 million. The monthly average of long-term liabilities to financial institutions and debenture holders in the first nine months of 2008 amounted to approximately NIS 6.347 billion.

The working capital deficit at September 30, 2008 amounted to approximately NIS 727 million, compared to NIS 1.307 billion in the corresponding period. The improvement is mainly due to the multi-channel television segment, where there was a decrease in deficit of approximately NIS 738 million, mainly from classification of bank loans as long-term loans, in view of compliance with the terms of the financing agreement with the banks and an improvement in the international communication and NEP segment in the amount of approximately NIS 123 million.

The improvement was partially offset by an increase in deficit in working capital in the domestic fixed-line communication segment.

The Board of Directors examined the projected cash flow of the Company, including credit sources and the possibility of a capital raising, and determined that the deficit in working capital does not indicate a problem in the Company's liquidity.

The aforementioned information includes forward-looking information based on the Company's assessments. The actual results may differ significantly from those assessments if a change occurs in one of the factors taken into account in making the assessments.

4. Group involvement in the community and donations

The Group is active in the community through contributions to recognized non-profit organizations that channel funds to education, welfare and other causes, as well as through development of direct volunteering of employees in the community. In the reporting period, Bezeq works with "Matan - Your Way to Give", a non-profit organization that assists companies in implementing their philanthropic vision. In addition, the Company has become a member of "Maale- Business for Social Responsibility", a non-profit membership organization that advocates corporate values. Additionally, Group employees volunteer in additional and diverse community involvement activities. During the reporting period, Group was involved in the community and donated approximately NIS 2.252 million.

5. Exposure to and management of market risks

A. Further to the description in the 2007 Directors' Report, hedging transactions against market risks concerning exposure to fluctuations in the exchange rate and the CPI partially reduced this exposure.

B. The sensitivity analyses for the fair value and the effect of the change in the market prices on the fair value of on- or off-balance sheet contractual agreements on September 30, 2008, are not substantially different from the December 31, 2007 statements. However, the total fair value of net liabilities that are sensitive to fluctuations in the dollar-shekel exchange rate on December 31, 2007 should amount to approximately NIS 1.148 billion. The sensitivity to changes in the dollar interest rate should amount to approximately NIS 622 million, due to the adjusted measuring of communications to space sections, which should amount to approximately NIS 611 million instead of approximately NIS 343 million.

C. The linkage base report on September 30, 2008 is not substantially different from the December 31, 2007 statement.

The excess monetary liabilities over monetary assets in or linked to foreign currency on September 30, 2008 amounted to approximately NIS 88 million in the Group. Forward currency transactions on September 30, 2008 amounted to approximately NIS 232 million. The transactions were also intended to hedge against off-balance sheet liabilities in or linked to foreign currency.

The excess liabilities on financial assets linked to the CPI on September 30, 2008 amounted to approximately NIS 5.818 billion in the Group. As a result of hedging transactions, on September 30, 2008 the net CPI-linked liabilities, which are not hedged by forward transactions, amounted to approximately NIS 4.619 billion.

6. Critical accounting estimates

Preparation of the financial statements according to IFRS requires the management to make estimates and assessments that influence the reported values of assets and liabilities, income and expenses, and disclosure relating to contingent assets and liabilities. Management bases its estimates and assessments on past experience and on additional factors, fair value assessments and opinions which it believes are relevant, taking circumstances into account. The actual results can differ from those assessments based on various assumptions and conditions. Information on the principal matters of uncertainty in critical assessments and judgments in the application of the accounting policies is provided in the annual financial statements. We believe that these assessments and estimates are critical because every change in them and in the assumptions has the potential to materially affect the financial statements.

7. Disclosure regarding the process for approval of the Company's financial statements

The Company organ given the responsibility for oversight is the Board of Directors. The Board of Directors appointed a balance sheet committee whose duties and composition are described in the 2007 Directors' Report.

The financial statements were discussed at the balance sheet committee and submitted to the Board of Directors for approval. The following officers attended the board discussion: Board members – Shlomo Rodav, Eyal Yaniv, Menachem Inbar, Michael Grabiner, Ran Gottfried, Yoav Rubinstein, Elon Shalev, Kihara Kiarie, David Gilboa, Rami Nomkin, Yitzhak Idelman, Yehuda Porat, Arieh Saban and Adam Chesnoff. In addition, the following officers attended: Avi Gabbay – CEO, Alan Gelman – Deputy CEO and CFO. Representatives of the Company's auditors, Somekh Chaikin, also participated in the discussion.

8. Sundry and events subsequent to the date of the financial statements

A. On June 1, 2008, the general shareholders meeting approved, this subsequent to the approval by the board of directors on April 17, 2008, the employment conditions for the chairman of the Board of Directors as described in Note 7 to the financial statements. The directors examined each component in the compensation package and the package as a whole, and in their opinion the general compensation package is appropriate and reasonable under the circumstances and is compatible with the nature of the position and the challenges facing the chairman and the expectations of the board. The compensation package was also compared to other large companies in Israel and was found to be within the high range of the benchmarks.

B. On September 28, 2008, the general meeting of the Company's shareholders (after approval of the Board of Directors and its Audit Committee) approved the extension of the Company's management agreement with a corporation connected to Ap.Sb.Ar. Holdings Ltd., the Company's controlling shareholder, for an additional three years subsequent to the expiry of the current agreement, under the same terms as the original agreement.

C. In the current quarter, following the global economic crisis, markets worldwide are slowing down and credit is being tightened. The expectation is that the effects of this process will continue to be felt throughout 2009 and a transition from growth to recession seems likely. The Israeli market will also suffer a significant slow-down and business activity and central economic parameters will worsen. The Company estimates that the crisis could have an adverse effect on its operations, but at this stage it is unable to assess the impact of the crisis on the activities of the Group.

The aforementioned information includes forward-looking information based on the Company's assessments. The actual results may differ significantly from those assessments if a change occurs in one of the factors taken into account in making the assessments.

D. At September 30, 2008, the Group's net dollar-linked contractual liabilities (including off-balance sheet) amounted to approximately NIS 909 million. The Group's net CPI-linked liabilities (including off-balance sheet) amounted to approximately NIS 5.517 billion. The dollar exchange rate rose by 16.7% between September 30, 2008, and the date of approval of the financial statements as well as the CPI which rose by 0.1% in October 2008.

E. The Company is exposed to changes in copper prices, resulting in a change in the scrap value of the Company's copper cable infrastructure. For further details, see Note 14(1) in the financial statements.

F. On June 26, 2008, the Company's Board of Directors adopted a policy for management of financial exposure, replacing the former exposure policy. The primary aim of the new policy is to reduce material exposure to market risks that will affect the Group's cash flows and financial results. Based on this policy, the Company will enter into hedging transactions, in part, according to the circumstances and its judgment, primarily to reduce its exposure to changes in the foreign currency exchange and the rate of the CPI.

We thank the managers of the Group companies, its employees and the shareholders.

Shlomo Rodav	**Avi Gabbay**
Chairman of the Board	**CEO**