D.B.S. Satellite Services (1998) Ltd.

Valuation of operations as of Dec. 31, 2018

March 2019

Prometheus
Financial Advisory

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Foreword and Limitation of Liability

Prometheus Financial Advisory Ltd. ("Prometheus" or "the Firm") was asked on December 9, 2018 by Sharon Jeno, CPA of D.B.S. Satellite Services (1998) Ltd. ("Yes" or "the Client" or "the Company") to prepare a valuation of the Company's operations as of December 31, 2018 ("the Valuation"). Our opinion is presented for the client's use only, and may be attached to its financial reports. No other use of this opinion will be allowed ,without prior written approval from the Firm.

Financial studies are designed to reasonably and fairly reflect a given state of affairs at a given time, based on known data and according to underlying assumptions, estimates and forecasts, including forward-looking information (as defined in the Securities Law, 1968) whose materialization is uncertain. As a result, this Valuation is only valid as of its signature date, and is based on information from the Company and/or persons acting on its behalf and additional sources such as financial statements, assessments, forecasts, and appraisals ("the Information"). The Valuation describes the Information, analyses and review procedures used in its preparation ,but this description is not necessarily full or detailed. It is emphasized that the Firm does not independently verify the Information, and assumes the Information is reliable. Thus, the Valuation does not verify the Information's accuracy or integrity and does not include an audit of its compliance with accounting principles. The Firm is not responsible for any implications of the Information's presentation methods (accounting or otherwise). The Information is partly based on existing knowledge as of the Valuation date, and on various assumptions and expectations concerning the Company and numerous external factors, including market conditions, existing and potential competitors, and general economic conditions. If the Information is found to be incomplete, inaccurate or unreliable, the results of the Valuation are liable to change, and so the Firm reserves the right to update the Work should any new Information arise. However, it is noted that the Firm is not aware of any matter which indicate that the Information is unreasonable.

It is clarified that the Firm has no dependence or vested interest in the Valuation, the Company and the Company's controlling shareholders, other than the fact that the Firm receives fees for this Valuation ,and such fees are not contingent on the results of the Valuation.

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It is noted that rounding of numbers may constitute an immaterial deviation when summing/multiplying the numbers presented in this Valuation.

Previous Valuations and Information Sources

Key Sources of Information Used in the Valuation:

- Yes's audited financial statements for 2015-2017 and the draft financial statements as of December 31, 2018
- Long-term forecast prepared by the Company's management
- Company valuation as of December 31, 2015
- Company valuation as of December 31, 2016
- Company valuation as of June 30, 2017, September 30, 2017, and December 31, 2017
- Valuation of Bezeq's holdings in Yes as of March 23, 2015
- Purchase Price Allocation (PPA) for Yes as of March 23, 2015
- Other financial data and various verbal clarifications received on demand
- Background data and market data, from public sources on the internet, news print, or other public sources
- Israel Central Bureau of Statistics and Bank of Israel data
- The Capital IQ system
- Discussions and meetings with Company staff

The Assessing Company

Prometheus Financial Advisory

Prometheus is a firm providing financial advisory services and expert opinions, led by Yuval Zilberstein, CPA, who serves as CEO; and Eyal Szewach, who serves as executive partner. The Firm consults clients on M&A transactions, and on significant projects across a diverse range of industries.

The study was conducted by a team headed by Eyal Szewach, founding partner in the Firm, who holds a bachelor's degree in electronic engineering from the Technion, and an MBA from Tel Aviv University. Mr. Szewach is an expert with over 10 years' experience in valuation, financial statement analysis, preparing expert opinions, and performing various financial advisory services for companies and businesses.

Sincerely,

Prometheus Financial Advisory Ltd.

March 27, 2019

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yes.

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Executive Summary

Company Overview

General

DBS Satellite Services (1998) Ltd. ("Yes" or "Multi-Channel Television Operations") was incorporated in Israel in 1998. Yes holds a Ministry of Communications license for satellite-based television broadcasts .

As of the end of the second quarter of 2018*, Yes's market share went down to 35%, from 37% at the end of 2017. This decrease was mainly due to entry of new competitors - Cellcom, Partner, Netflix, and others.

HOT is the company with the largest share of the multi-channel television market - 47% as of the second quarter of 2018. Together with Cellcom's 12% share, they are Yes's main competitors in this market.

Yes's revenues are derived from the following sub-segments:

Multi-channel television - Yes offers a broad range of 150 different channels including 30 high-definition (HD) channels, radio channels, and interactive services.

*.Data refer to Q2/2018, as this was HOT's last report. Subsequently, HOT"s statements were published as part of Altice's reports which are unusable for our purposes .

Advanced services - Yes offers various advanced satellite set-top-boxes (STBs), which allow pre-recording content and high-resolution broadcasts

Furthermore, Yes offers a multi-room service, which allows content recorded on a recording STB to be viewed on non-recording STB over the home network. Yes's customers also have free access to the yesGo application, and to Primetime and Start Over services .

VOD - Yes offers video on demand content through internet-connected STBs.

Sting TV - OTT television services offering a selection of plans and VOD services, connected through a streamer. Sting TV competes at a lower price point and is the Company's response to other streaming services.

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Executive Summary

Results of Valuation

Valuation under the DCF model

Results of valuation	NIS millions
Portion of EV attributed to Modeled Years	(741)
Portion of EV attributed to the representative year	(130)
Total EV	**(871)**

As of December 31, 2018, the DCF model yields a negative enterprise value for the Company, of NIS (871) million ,compared to a book value of NIS 886 million .

A key assumption underlying the forecast is that future technology will be interactive and bi-directional, and that satellite products cannot compete with IP products over time due to the growing gap in customer experience. As a result, the long-term forecast reflects a gradual migration (from satellite broadcasting to internet-based broadcasting). Thus, we assumed a gradual replacement of satellite STBs with IP STBs, upgrades to broadcasting infrastructure, building customer service support infrastructure, and adjustment of content contracts to OTT broadcasting. These conditions, coupled by expectations for continued competition throughout the forecast period and a relatively inflexible cost structure have led us to project . significant operating losses and negative cash flows in the coming years, before and so long as the Company completes the shift in its technological and business model

After migrating from satellite to IP-based transmission, Yes's satelliite segment costs will be replaced with transmission costs inside the Group. Thus, cash flows will increase at the Group level, as compared to continued reliance on satellite infrastructure. Therefore, in terms of its consolidated financial statements, Bezeq views Yes as having value beyond it's stand-alone share value.

In light of the negative enterprise value, accounting standards mandate that Yes be valued using the net asset value method.

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Executive Summary

Results of Valuation

Valuation results under NAV requirements

Details / NIS millions	Balance sheet value as of Dec. 31, 2018	Write-off	Disposal value	NAV
Cash and cash equivalents	80	-	80	-
Trade receivables	132	-	132	132
Other receivables	8	-	8	8
Broadcasting rights	463	(403)	60	60
Property, plant and equipment	672	(559)	113	113
Intangible assets	107	(106)	1	1
Subscriber acquisition	29	*(29)	-	-
Real estate asset usage rights	84	-	84	84
Vehicle lease usage rights	31	**(3)	28	28
Total assets	**1,606**	**(1,100)**	**506**	**425**
Bank credit	(14)	-	(14)	-
Current maturities on debentures	(8)	-	(8)	-
Trade payables	(440)	-	(440)	(440)
Other payables	(64)	-	(64)	(64)
Provisions	(19)	-	(19)	(19)
Bank loans	(7)	-	(7)	-
Other liabilities	(10)	-	(10)	(10)
Employee benefits	(4)	-	(4)	-
Real estate leasing liabilities	(86)	-	(86)	(86)
Vehicle leasing liabilities	(35)	-	(35)	(35)
Total liabilities	**(687)**	**-**	**(687)**	**(654)**
Equity	**919**		**(181)**	**(229)**
Excess of cost - goodwill for Yes recognized in Bezeq's books	33	(33)	-	-
Excess of cost - customers	266	(266)	-	-
Excess of cost - brand	238	(238)	-	-
Excess of cost - tax reserve (net of excess of cost on tax reserve for debentures)	(116)	116	-	-
Total	**1,340**	**(1,521)**	**(181)**	**(229)**

Under this approach ,the net disposal value of the Company's assets were valued as follows:

Thus, Yes's equity, as derived from the fair value of balance sheet items revalued according to IAS 36 and IFRS 15, is negative 229 million NIS.

*Outside the scope of IAS 36; presented for the sake of convenience to clarify the overall picture.

**The asset's presentation method was provided by the Company.

Executive Summary

Changes in Yes's Value

Changes in Yes's value

Changes in Yes's value over time:

Details	NIS millions	Details
Yes valuation as of Mar. 23, 2015	2,496	Fahn Kanne valuation from May 19, 2015
Yes valuation as of Dec. 31, 2015	2,620	Giza valuation from Mar. 9, 2016
% Change	5.0%	
Yes valuation as of Dec. 31, 2016	2,551	Giza valuation from Mar. 28, 2017
% Change	(2.6%)	
Yes valuation as of Jun. 30, 2017	1,947	Giza valuation from Aug. 23, 2017
% Change	(23.7%)	
Yes valuation as of Sept. 30, 2017	1,761	Giza valuation from Nov. 27, 2017
% Change	(9.6%)	
Yes valuation as of Dec. 31, 2017	1,346	Prometheus valuation from Mar. 28, 2018
% Change	(23.6%)	
Yes valuation as of Dec. 31, 2018	(229)	Prometheus valuation (NAV) from Mar. 18, 2019
% Change	(117.0%)	

The Company is characterized by increasingly high inflexible costs in its content category and in significant investments in non-consumable equipment (mainly STBs). The Company was unable to adjust its costs to changing market conditions, and so subscriber attrition and changes in ARPU, along with heavy investments and significant content expenses, directly reflect in its cash flow and lead to the sharp drop in the Company's value.

Executive Summary

Yes's Operations – 2017 Forecast for 2022 vs .Current Forecast for 2022

Details / NIS millions	2022 forecast (Dec. 31, 2017*)	2022 forecast (current forecast)	Difference
Total revenues	**1,457**	**1,297**	**(160)**
Total operating expenses	**1,309**	**1,464**	**155**
%of revenues	89.8%	112.8%	
Other income (expenses), net	0	0	0
Operating profit	**148**	**(167)**	**(315)**
%of revenues	10.2%	(12.8%)	
Depreciation and amortization	236	303	67
EBITDA	**384**	**136**	**(248)**
%of revenues	26.5%	10.6%	
CAPEX	177	231	54
%of revenues	12.2%	17.8%	
EBITDA - CAPEX	**207**	**(95)**	**(302)**
%of revenues	14.3%	(7.2%)	

*Based on Yes's management's forecast used in the valuation as of Dec. 31, 2017

The table presents Yes's management's forecast for 2022 (including Sting operations), used in the valuation as of Dec. 31, 2017, compared with the current valuation used in the financial statements as of Dec. 31, 2018.

The change in the forecast is mainly due to a shift in the Company's view concerning the relevant technology in the future and consumer preferences, continuing through the plan to transition to OTT broadcasting. As a result, the forecast assumes a plan for gradual migration to IP, which should be completed at the end of 2025. Implementing this plan requires replacement of most Company STBs, and maintaining current expenses during the transition period for both operations (satellite and IP).

Analysis of the differences between the forecasts:

- **Revenues:** Despite the forecast growth in revenues from Sting, the Company's revenues went down in the updated forecast. The difference totals NIS 160 million (a change of 11%), and is due to increased competition leading to a higher attrition rate of premium customers compared to previous estimates, along with lower ARPU.

Executive Summary

Yes's Operations – 2017 Forecast for 2022 vs .Current Forecast for 2022

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*Based on Yes's management's forecast used in the valuation as of Dec. 31, 2017

- **Operating expenses :**Operating expenses are NIS 155 million higher in the current forecast over the previous forecast (difference of 11.9%), mainly due to higher content costs following price hikes in the content market. OPEX also grew due to sports rights which are now estimated at a higher point than in the previous forecast due to continued price increases on rights (derived from the RGE agreement - additional cost for the Champions League, payment for each Sting customer) - an additional NIS 50 million in cost in 2021. The upward adjustment was also due to other operating expenses due to the simultaneous operation of two broadcasting methods (satellite and IP).
- **EBITDA:** Changes in revenues and expenses drove down the Company's EBITDA (a difference of NIS 248 million).
- **CAPEX:** The gradual migration to IP-based broadcasting means that, in 2022, the Company is investing simultaneously in two operating platforms (satellite and IP), increasing CAPEX over the previous forecast.
- **Operating cash flow:** Operating cash flow (before changes in operating working capital and tax expenses), as reflected in **EBITDA minus CAPEX**, decreased and the Company adjusted its results downward by NIS 302 million over the previous forecast (difference of 220%).

Prometheus Financial Advisory

Chapter 1 – Description of the Company's Business

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Description of the Company's Business

General

DBS Satellite Services (1998) Ltd. ("Yes" or "Multi-Channel Television Operations") was incorporated in Israel in 1998. Yes holds a Ministry of Communications license for satellite-based television broadcasts .

Until March 25, 2015, Bezeq held 49.78% of Yes's issued capital, and warrants to an additional 8.6%. Yes's remaining share capital was held by Eurocom D.B.S. Ltd. On March 25, 2015, Bezeq exercised its warrants, without payment, and on June 24, 2015, it bought all of Eurocom D.B.S.'s holdings in Yes along with the shareholder loans which Eurocom Communications Ltd. (the controlling shareholder in Bezeq) had extended to Yes.

As of the end of the second quarter of 2018, Yes's market share went down to 35%, from 37% at the end of 2017. This decrease was mainly due to entry of new competitors - Cellcom, Partner, Netflix, and others.

HOT is the company with the largest share of the multi-channel television market - 47% as of the second quarter of 2018. Together with Cellcom's 12% share, they are Yes's main competitors in this market.

Yes's revenues are derived from the following sub-segments:

- **Multi-channel television** - Yes offers a broad range of 150 channels, such as: sports, nature, science and history, movies, series, kids and teens, music, recreation and lifestyle, foreign language channels, etc. Yes also offers some 30 high-definition (HD) channels, radio channels, and interactive services. Some of these channels are included in basic and entry-level bundles, and some are purchased by customers specifically in addition to the basic and entry-level bundles. In January 2018, Yes launched a new service - Yes Ultimate - a bundle comprising most content channels, premium channels, an enhanced STB, VOD, and additional services, for NIS 199 a month, including VAT. It is noted that Yes's current plans charge additional fees above the basic plan price for additional STBs.

Description of the Company's Business

- **Advanced services** - Yes offers various PVR satellite STBs, which allow pre-recording of content. Yes also offers HD Zapper boxes (yesHD), which support HD broadcasting; HDPVR boxes, which support both recording and HD broadcasting; and 4K boxes (yes Ultra), which support 4K broadcasting and recording. Furthermore, Yes offers a MultiRoom service, which allows content recorded on a recording STB to be viewed on non-recording STBs over the home network. Some customers also receive free use of the yesGo app, which delivers a range of television channels for viewing on smartphones, tablets, and various compeuters. Finally, Yes offers Primetime and Start Over services.
- **VOD** - Yes offers video on demand content through internet-connected STBs.
- **Sting TV** - OTT television services offering a selection of plans and VOD services, connected through a streamer. Sting TV competes at a lower price point and is the Company's response to other streaming services.

Yes - Key Performance Highlights (KPIs)

Figure 1: Yes - KPIs

yes KPI's	Note	2016	2017	2018
Subscribers (thousands)	1	614	587	574
%Change		(3.3%)	(4.4%)	(2.3%)
ARPU	2	233	228	211
%Change		0.3%	(2.2%)	(7.5%)

1. The number of Yes multi-channel television subscribers is shrinking, due to new competitors and substitute services such as Cellcom TV, Partner TV, traditional competition from HOT, competition from streaming services (Netflix and others) and pirated content.
2. ARPU is also shrinking, due to increasing competition. As a result, the Company decided to lower its prices (e.g. - the Company's 'Ultimate' initiative which included price cuts).

Chapter 2 - Television Services Market

Chapter 2 - Television Services Market

The Television Services Market in Israel

Television services market - general

The television market has seen significant disruption in recent years. The two, established, market players are Yes (which provides satellite-based television services), and HOT (which provides cable-based television services).

In addition to these companies, the Second Authority for Television and Radio operates a DTT network (Idan+), offering a basic channel bundle for free, other than the cost of buying the STB for the service .

The increase in the bandwidths of communication infrastructures in Israel, alongside technological improvements enabling the transmission of video content over the internet and cellular networks and improved compression capabilities enable wider use of these infrastructures for the transmission of video content.

These technological changes have allowed other telecom companies - Cellcom and Partner - to enter this market and offer television services without setting up infrastructure such as Yes and HOT needed to do. In addition to Israeli companies, global companies offer VOD services through internet streaming services, such as Netflix and Amazon Prime. These companies also constitute an ever-increasing competitive force. Furthermore, an effective and enforceable solution has yet to be found for widespread use of pirated content.

Competition and recent developments

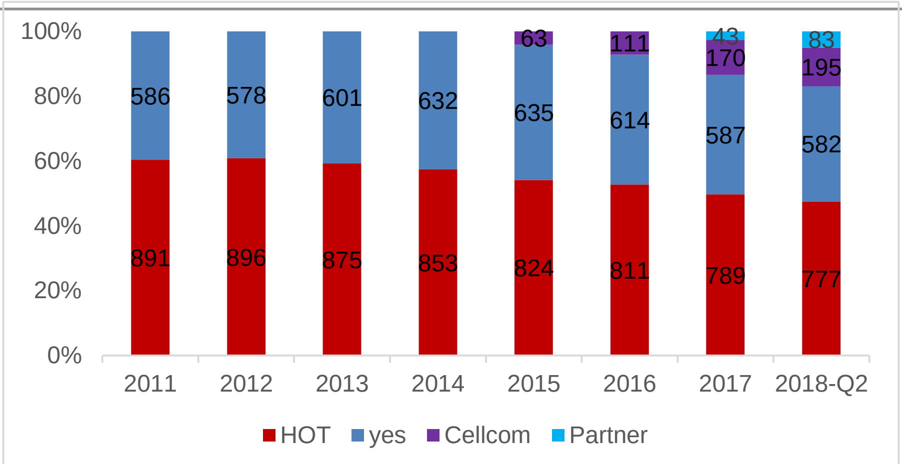
Competition in the television market focuses on content, pricing, service quality, and add-on service offerings such as HD, VOD and advanced STBs. Competition is driven by demand for advanced and personalized television services.

HOT and OTT providers

The two main market players are Yes and HOT. In recent years, HOT's market share has gone down, despite their bundle offering. Furthermore, Yes's market share, which saw an upward trend until 2015, has eroded in recent years, mainly due to the introduction of Cellcom TV. In June 2017, Partner also began to offer IPTV services, uner the Partner TV brand .

The Television Services Market in Israel

Figure 2: Television service subscribers[15]



As the above chart demonstrates, competition and changes in the television market have reduced the number of both HOT and Yes subscribers, from Yes's 587,000 and HOT's 789,000 in 2017, to Yes's 582,000 and HOT's 777,000 in Q2/2018. Prices for Cellcom and Partner's content bundles are significantly lower than Yes and HOT's, including due their lower investment in infrastructure (OTT operating model) and content. Furtherore, Cellcom and Partner can offer full telecom service offerings (quatro), which Yes and HOT cannot offer for regulatory reasons. Yes is also at a disadvantage against HOT and the other competitors as it cannot offer locked triple bundles, due to regulatory restrictions.

- Sting: Sting TV is Yes's OTT television service, which was launched in November 2017. The service includes a range of bundle options and VOD services, and is based on a streamer box. Sting TV competes at a lower price point and is the Company's response to other OTT and streaming services.

Streaming services

- Netflix: At the start of 2016, Netflix (the leading video content provider in the US) began allowing Israeli customers to subscribe to its services, causing a change in customer preferences.
- Netflix is a VOD platform which allows access to content from computers, mobile phones, smart TVs, and tablets, without an STB .
- Netflix is improving its ability to provide content to Israeli customers, and is a growing threat to traditional content providers. However, it currently mostly serves as a complementary, and not a substitute, product.

15. From Bezeq, Cellcom, Partner, and HOT's financial statements.

Chapter 2 - Television Services Market

The Television Services Market in Israel

- NEXT TV: HOT's streaming service, launched in August 2017 in response to increasing competition and as a supplementary offering to customers seeking basic low-cost services.
- Other streaming providers: In Israel and abroad, and especially in the US, other providers such as Amazon Prime offer streaming services, and constitute a potential threat to the local market.

Regulation

Multi-channel television broadcasts by satellite and cable are subject to the Communications Law and the corresponding rules and regulations, in addition to the provisions of the broadcasting licenses and the Satellite and Cable Broadcasting Commission's decisions. As such, the market is subject to several regulatory restrictions, including:

- No advertising: In Israel, advertising is banned on cable and satellite channels, in contrast to global market practice.
- Investment in original content: According to the Commission's decision of November 2015, the minimum amount for investment in original Israeli content will increase in 2017 from 8% of annual revenue from subscription fees, to 9%. Bezeq clarified that, at this time, the Commission has decided not to implement the change in 2017 and 2018. It is noted that, in June 2016, the Filber Committee recommended that, in the coming years, Yes and HOT's requirement to invest in original content should decrease to .6.5%
- Canceling early termination penalties for broadcast service contracts: License-holders are prohibited from signing consumers on long-term contracts whose violation incurs penalty payments.
- Tariff regulation: Companies must report to the Commission on changes in Commission-approved prices, and the Commission chairman may prohibit such change under the terms specified in the license.

Key data on the US Pay TV market[1]

Figure 3: Change in subscribers to the 12 leading companies in the US

	Q3 2018
Multi-channel television subscribers in the US	90,324,721
Change from same quarter in 2017	(974,291)

Figure 4: ARPU for the leading companies in the US (USD)[2]

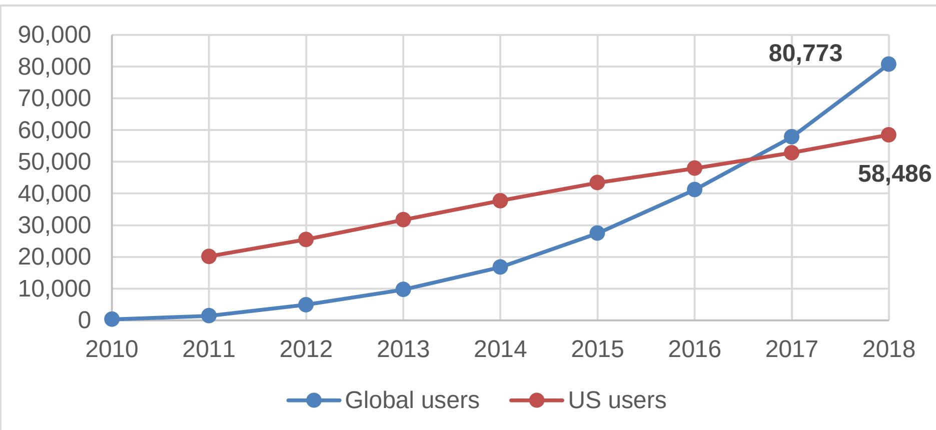
ARPU, USD	*YoY change*	2016	2017
DISH	(2.52%)	88.66	86.43
AT&T	1.88%	119.00	121.24
Cablevision	2.97%	106.63	109.79
Charter (Residential)	3.32%	81.13	83.82
Comcast	3.71%	82.21	85.26
Average	2.00%	95.91	97.82

1. *Source: Leichtman Research Group*
2. *Source: The companies' annual reports*

Television Services Market in Israel - Netflix

Netflix's entry to the market

Figure 5: Paid netflix subscribers (thousands)[3]

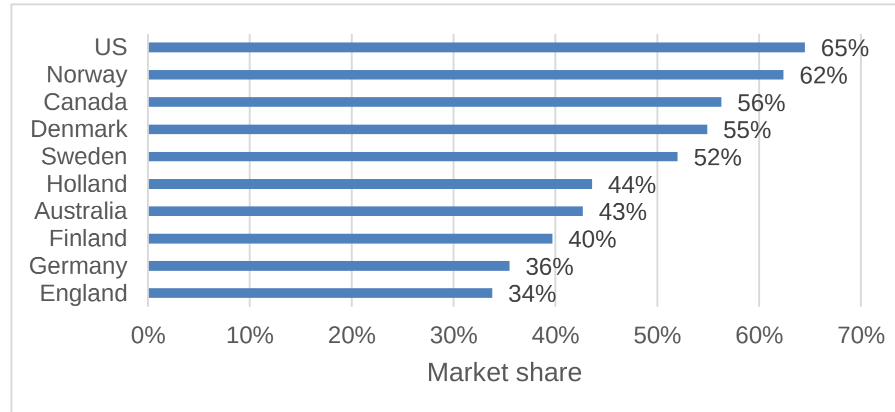


- Netflix started offering streaming services in the US in 2007. As of the end of 2018, the company recruited 139 million users worldwide, of which 58 million in the US alone - accounting for 64.5% of the paid market in the US.
- Netflix offers OTT VOD services. The company buys or produces original content at a total cost of USD 13 billion, as of 2018.

3. *Source: Netflix's financial statements*

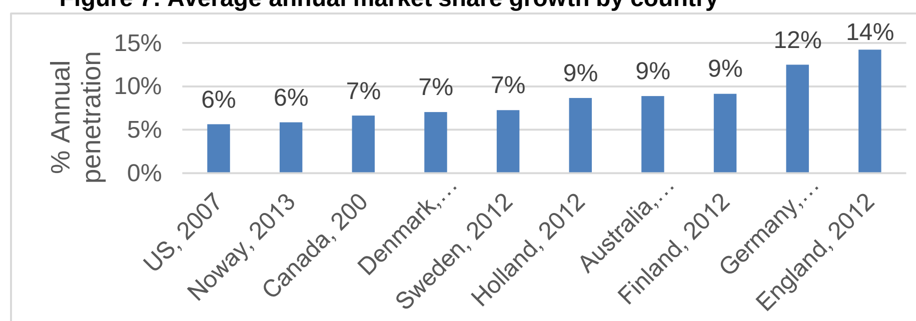
Netflix's new market penetration rate

Figure 6: 10 countries in which Netflix holds the largest market share[4]



Netflix's market share ranges from 34% to .65%

Figure 7: Average annual market share growth by country[5]



Netflix's average annual penetration rate ranges from 6% to 14%. Notably, Netflix first entered Australia in 2015, and in 2018 it already holds 43% of the market.

4. *Source: Estimates 2018eMarketer*

5. *Source: Netflix's financial statements*

Chapter 2 - Television Services Market

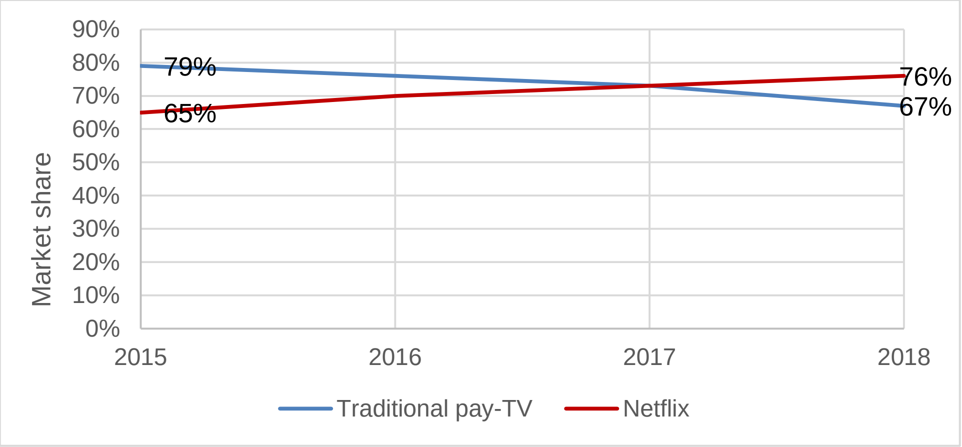
Television Services Market in Israel - Netflix

Netflix's impact on the Israeli market

Netflix first launched in Israel in 2017, and in its first year already gained 7% of the market. In 2018, it increased its market share by 11%.

Netflix's impact on US broadcasters

Figure 8: US broadcast market share[7]



Between 2015 and 2017, Netflix caused a 12% decrease in the traditional TV companies' market share, while its own market share grew 11%.

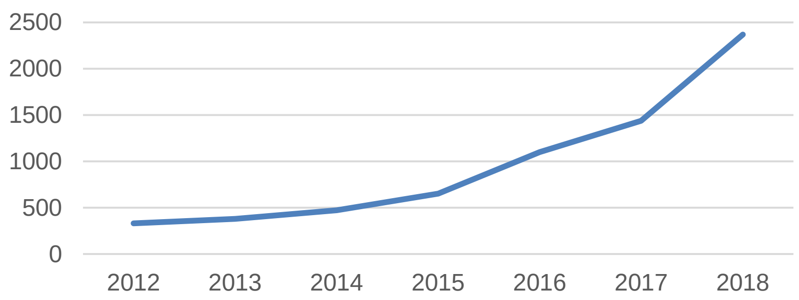
6. *Yes and HOT's financial statements*

.7Source: PwC – Video Consumer Motivations 2018

Television Services Market in Israel - Netflix

Netflix's operating expenses

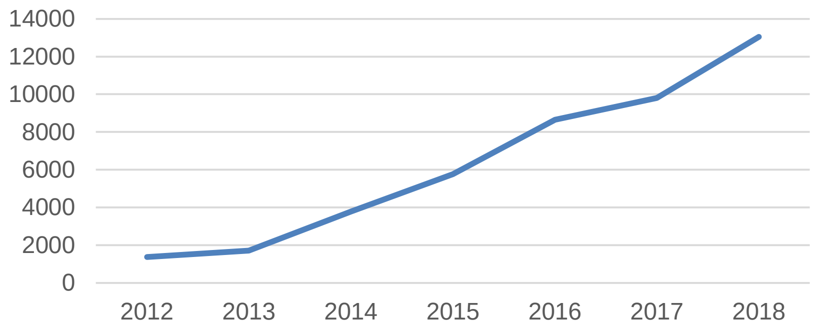
Figure 9: Netflix's expenses on technology (USD millions)[8]



Netflix's expenditure on technology has grown in recent years. For example, in 2017-2018 technology expenses grew by USD 933 million, or 65% YoY (15% of its revenues in 2018, as compared to 13% of its revenues in 2017).

8. Source: Netflix's financial statements

Figure 10: Netflix's expenses on content (USD millions)[9]



Between 2012 and 2018, Netflix's content expenses grew from USD 1,368 million to USD 13,043 million - or 850% in 6 years. On average, Netflix spends 86% of its revenue on content.

These expenses match Netflix's philosophy that its competitive advantages depend on its ability to provide a user experience which differentiates it from the competition. This is evident in the growth in its content and technology expenditure.

.9Source: Netflix's financial statements

Chapter 3 - Financial Statement Analysis

Balance Sheet - Multi-Channel Television Operations (Yes)

Yes's audited data for Dec. 31, 2015-2017, from its draft financial statements as of Dec. 31, 2018:

NIS millions	December 31, 2015 Audited	December 31, 2016 Audited	December 31, 2017 Audited	December 31, 2018 Draft*
Assets				
Current assets				
Cash and cash equivalents	95	142	112	80
Deposits	50	-	-	-
Trade receivables	159	155	142	132
Other receivables	15	143	6	8
Inventory	-	-	9	-
	319	**440**	**269**	**220**
Non-current assets				
Broadcasting rights	445	421	448	463
Property, plant and equipment	770	707	644	672
Intangible assets	133	127	141	136
Deferred taxes	-	331	-	-
Usage rights in leased assets	-	-	-	115
	1,348	**1,586**	**1,233**	**1,386**
Total assets	**1,667**	**2,026**	**1,502**	**1,606**

* 2018 data are based on the draft financial statements before write-downs.

Assets - Key Items

Current assets: In 2018, the change in the Company's cash balances was mainly due to changes in Bezeq's investments in the Company's equity .

Non-current assets:

- Broadcasting rights: Yes holds two kinds of broadcasting rights:
  1. Broadcasting rights bought from content providers (movies and series).
  2. Broadcasting rights for original content in which the Company invests directly.

  This asset routinely serves the Company's operations, and so is part of the segment's operating working capital.
- Property, plant and equipment: Yes's PP&E consists of broadcasting and receiving equipment, office equipment and furniture, improvements to rented properties, and the bulk of its PP&E is attributable to discounted installation costs and satellite decoders (STBs). Yes's remaining PP&E balance grew in 2018, mainly due to a greater investment in STBs and streamers.
- Usage rights in leased assets: This item grew following the first-time application of IFRS 16.

Chapter 3 - Financial Statement Analysis

Balance Sheet - Multi-Channel Television Operations (Yes)

NIS millions	December 31, 2015 Audited	December 31, 2016 Audited	December 31, 2017 Audited	December 31, 2018 Draft*
Liabilities + equity				
Current liabilities				
Credit	15	15	14	14
Current maturities on debentures	382	383	216	8
Trade payables	399	463	479	440
Other payables	73	83	86	64
Interest on debentures and loans	22	-	4	-
Provisions	12	6	5	19
Liabilities for leases	-	-	-	30
	903	**950**	**804**	**575**
Non-current liabilities				
Bank loans	49	34	20	7
Debentures	828	435	218	-
Loans from shareholders	4,890	-	95	-
Other long-term liabilities	11	12	14	10
Employee benefits	4	3	3	4
Liabilities for leases	-	-	-	91
	5,782	**484**	**350**	**112**
Equity	**(5,018)**	**592**	**348**	**919**
Total liabilities + equity	**1,667**	**2,026**	**1,502**	**1,606**

Liabilities and Equity – Analysis of Key Items

Trade payables: The decrease in trade payables in 2018 was mainly due to increased payments to suppliers (including original content providers and the sports channel).

Debentures: In 2017, most debentures (96%) were held by Bezeq, while in 2018 Bezeq converted its debenture holdings (96%) to equity.

Loans from shareholders: The balance of Bezeq's loans to Yes was converted to equity.

* 2018 data are based on the draft financial statements before write-downs.

Chapter 3 - Financial Statement Analysis

Income Statement - Multi-Channel Television Operations (Yes)

NIS millions	2015 Audited	2016 Audited	2017 Audited	2018 Draft*
Revenues	1,774	1,745	1,650	1,473
YoY change	**2.9%**	**(1.6%)**	**(5.5%)**	**(10.7%)**
Operating general and salary expenses	1,201	1,196	1,202	1,219
%of revenues	67.7%	67.9%	72.8%	82.8%
Depreciation and amortization	322	296	285	293
%of revenues	18.2%	17.0%	17.3%	19.9%
Total operating expenses	**1,523**	**1,492**	**1,487**	**1,512**
Other income (expenses), net	-	11	-	(17)
Operating profit	**250**	**264**	**163**	**(56)**
%of revenues	**14.1%**	**15.1%**	**9.9%**	**(3.8%)**
Depreciation and amortization	322	296	285	293
Adjusted EBITDA	**572**	**560**	**448**	**237**
%of revenues	**32.3%**	**32.1%**	**27.2%**	**16.1%**
CAPEX	265	208	233	297
%of revenues	14.9%	11.9%	14.1%	20.2%
EBITDA - CAPEX	**308**	**352**	**215**	**(60)**

* 2018 data are based on the draft financial statements before write-downs and adjustment of lease expenses under IFRS 16.

Analysis of key items

Revenues

Revenues were down in 2018 (by 10.7%) due to lower plan prices (launch of Ultimate), and a decrease in the subscriber base.

Expenses

Content expenses continued rising in 2018 following the increase in contract prices (mainly sports).

Salary expenses were down in 2018 due to the Company's streamlining efforts, which will continue in the coming years.

Chapter 3 - Financial Statement Analysis

Income Statement - Multi-Channel Television Operations (Yes)

Analysis of key items (contd.)

CAPEX, EBITDA, and operating cash flows

EBITDA was down in both absolute value and as a percentage of revenues, from NIS 448 million in 2017 (27.2% of revenues), to NIS 237 million (16.1% of revenues) in 2018. **EBITDA** was down mainly due to lower revenues which was almost fully translated to profits due to the inflexible expense and investment structure. However, there was a NIS 65 million increase in **CAPEX**, mostly due to acceleration of STB purchases following a change in the satellite STB supplier, and the purchase of streamers for streaming services. Operating cash flows before taxes and changes in operating working capital, as reflected in **EBITDA minus CAPEX**, was down by NIS 276 million YoY, totaling NIS (60) million (13% of revenues) in 2018, compared to NIS 216 million in 2017.

Chapter 4 - Valuation

Chapter 4 - Valuation

Valuation Method - Multi-Channel Television Operations (Yes)

General

The OTT revolution lowered market entry barriers, and led Cellcom and Partner to enter the market with low-cost content offerings. Furthermore, the entry of content giant Netflix into the market, which broke the traditional value chain, significantly increased competition (as detailed in Chapter 2, pages 16-18). These changes reduced Yes's subscriber base. In order to stop this hemorrhaging, Yes decided to significantly cut its prices without being able to significantly cut its costs. Since the Company is operationally leveraged, any decrease in revenues fully translates into its profits. Due to the smaller customer base and lower price points, the Company's revenues shrank, while content costs grew, which led Yes to incur operating losses and negative cash flows .

Technological infrastructure upgrade

The Company's management believes that, over time, the existing technological infrastructure will not be able to provide an adequate solution to customer needs compared to market alternatives. Due to the need to upgrade its infrastructure, the Company believes that IP technology would be able to maximize customer needs and the Company's operating metrics. The migration between infrastructures will be gradual, between 2019-2025, and will add significant transmission costs in the short and medium terms. After migrating from satellite to IP-based transmission, Yes's satelliite segment costs will be replaced with transmission costs inside the Bezeq Group. Thus, consolidated cash flows will increase as compared to continued reliance on satellite infrastructure.

Key Assumption

In light of structural market changes, increasing competition, and major changes in its technological model, the Company is expected to incur operating losses and negative cash flows until completing its migration to IP. In 2026, upon completing its migration to the new network, the Company expects a minor negative cash flow, near the break-even point. In light of this forecast, the valuation covers the period of 2019-2026, with the representative year being after completing the tech migration and cessation of space segment payments .

Chapter 4 - Valuation

Multi-Channel Television Operations (Yes) - Key Assumptions

Revenues

- Subscribers: We assumed that the Company's overall subscriber base would grow from 574,000 as of the end of 2018, to 667,000 by the end of 2026. However, a significant change will occur in the breakdown of customers between satellite/premium customers and Sting customers. Sting customers will account for an ever-growing portion of the Company's subscriber base, from a negligible percentage as of the end of 2018, to the largest segment by the end of 2026. It is noted that these forecasts account for the tendency of most consumers to use Netflix as a supplementary, and not a substitute, service to traditional pay-TV services. This assumption must be periodically reviewed according as consumer preferences develop.

- ARPU: Competition in the television market has led the Company to implement two key initiatives, each of which lowered ARPU in 2018:

  a. Introducing Yes Ultimate for satellite subscribers - offering customers services which were previously subject to additional payment, such as premium channels and VOD services.

  b. Sting TV - Yes launched its OTT service to offer an alternative to competition in the lower cost points, which mostly comprises other OTT players.

According to Yes management's forecast, which was reviewed and found reasonable, working assumptions for ARPU are as follows:

a. **Premium ARPU** - Market competition will continue to erode ARPU over time.

b. **Low-cost ARPU** - ARPU will gradually grow until 2024. It is noted that this assumption was found reasonable in light of our assessments that present prices in the low-cost market are not sustainable over time, and the Company's corresponding focus on broader content bundles offering additional content and enhanced sales. Moreover, sports channels in the bundle make the offering more attractive to customers.

In summary, Company revenues will gradually shrink from NIS 1,473 million in 2018 to NIS 1,270 million in 2026, with satellite/premium revenues continuing to erode with growth in low-cost service revenues partially making up the difference.

Chapter 4 - Valuation

Multi-Channel Television Operations (Yes) - Key Assumptions

KPIs and revenues

Year	2018A	2019E	2020E	2021E	2022E	2023E	2024E	2025E	2026E
Subscribers (thousands)									
Subscribers, end of period	574	587	592	602	617	637	652	667	667
%Change	(2.3%)	2.2%	0.9%	1.7%	2.5%	3.2%	2.4%	2.3%	0.0%
APRU (NIS/month)									
Weighted ARPU	211	197	190	183	177	171	166	161	159
%Change	(7.5%)	(6.6%)	(3.5%)	(3.5%)	(3.2%)	(3.4%)	(3.2%)	(3.1%)	(1.3%)
Revenues (NIS millions)									
Revenues	1,473	1,375	1,344	1,313	1,297	1,289	1,283	1,272	1,270
%Change	(10.7%)	(6.7%)	(2.3%)	(2.3%)	(1.2%)	(0.6%)	(0.5%)	(0.9%)	(0.2%)

Multi-Channel Television Operations (Yes) - Key Assumptions

Operating expenses

The Company's forecast for its operating cash flow expenditure in 2018-2026 is as follows:

Year	2018A	2019E	2020E	2021E	2022E	2023E	2024E	2025E	2026E
Cash flow expenditure*	**1,236**	**1,248**	**1,236**	**1,213**	**1,160**	**1,145**	**1,164**	**1,181**	**1,113**

*Operating expenses, including lease payments

The downward trend in expenses is mostly due to reduced salary costs in the short and medium terms from downsizing efforts under the Company's streamlining plan which are under negotiation with the workers' union, and which in light of the Company's position we assumed would be implemented in full. Expenses will also decrease due to lower content costs after 2021. It is noted that the increase in other operating expenses is due to increased network traffic costs as part of the transition to IP. The downward trend in expenses matches the change in Yes's satellite/premium and Sting customer base in the coming years .

Multi-Channel Television Operations (Yes) - Key Assumptions

EBITDA

The adjusted EBITDA forecast (including lease payments), as derived from the above revenue and expense assumptions, is as follows:

NIS millions	2018A	2019E	2020E	2021E	2022E	2023E	2024E	2025E	2026E
Adjusted EBITDA	**237**	**128**	**107**	**100**	**137**	**144**	**119**	**91**	**157**
%of revenues	16.1%	9.3%	8.0%	7.6%	10.6%	11.2%	9.3%	7.1%	12.4%

EBITDA will decrease in the next three years, reaching NIS 100 million in 2021 (7.6% of revenues). From 2022, we assume a recovery, with EBITDA totaling NIS 137 million (10.6% of revenues) in 2022. Afterward, in 2024-2025, we assumed another decresae in EBITDA due to the accelerated migration to IP, and a recovery in 2026 once space segment payments have stopped.

Tax expenses

We assumed a 23% corporate tax rate, according to the current statutory rate in Israel. Since the Company will run at a loss in the coming years, it is not expected to pay taxes over the forecast period. Since no profit is expected in the foreseeable future, no tax shield will be created from losses.

Multi-Channel Television Operations (Yes) - Key Assumptions

CAPEX

The Company's CAPEX forecast, as adopted, is as follows:

Year	2018A	2019E	2020E	2021E	2022E	2023E	2024E	2025E	2026E
Total CAPEX, net	**297**	**298**	**301**	**241**	**231**	**283**	**278**	**259**	**178**
%of revenues	20.1%	21.7%	22.4%	18.4%	17.8%	22.0%	21.7%	20.4%	14.0%

The Company estimates that CAPEX will decrease in 2021-2022 due to market saturation of advanced STBs, which will lead to a decrease in STB purchases and installations.

In subsequent years, CAPEX will increase from market penetration of streamers (IP boxes) and the costs required to maintain both satellite and IP operations. Later, investments are expected to decrease due to two factors:

1. The significantly lower cost of streamers compared to STBs.
2. Ramp-down of satellite operations, ceasing the simultaneous maintenance of both operations (satellite and IP).

Multi-Channel Television Operations (Yes) - Key Assumptions

Operating working capital

Assumptions concerning changes in operating working capital match Company projections .

Discounting rate and permanent growth

Under the CAPM model, the discounting rate applicable to Yes's operations is 8.35% (for details, see Appendix A). Since we believe the risk in these operations will not decrease compared to 2017, we used an 8.5% discounting rate, similar to the rate used in the previous valuation of the Multi-Channel Television segment .

We assumed a permanent growth rate of 0%.*

*Since the Company's cash flow is negative, we assumed that a company with a negative cash flow will not increase its negative cash flow.

Chapter 4 - Valuation

Multi-Channel Television Operations (Yes) - Projected Cash Flows

NIS millions	2015A	2016A	2017A	2018A	2019E	2020E	2021E	2022E	2023E	2024E	2025E	2026E	TY
Total revenues	**1,774**	**1,746**	**1,650**	**1,473**	**1,375**	**1,344**	**1,313**	**1,297**	**1,289**	**1,283**	**1,272**	**1,270**	**1,270**
%change from previous period		(1.6%)	(5.5%)	(10.7%)	(6.6%)	(2.3%)	(2.3%)	(1.2%)	(0.6%)	(0.5%)	(0.9%)	(0.2%)	0.0%
Total operating expenses (less depreciation and amortization)	**(1,201)**	**(1,186)**	**(1,201)**	**(1,236)**	**(1,248)**	**(1,236)**	**(1,213)**	**(1,160)**	**(1,145)**	**(1,164)**	**(1,181)**	**(1,113)**	
%of revenues	67.7%	67.7%	72.8%	83.9%	90.7%	92.0%	92.4%	89.4%	88.8%	90.7%	92.9%	87.6%	
Adjusted EBITDA	**572**	**560**	**448**	**237**	**128**	**107**	**100**	**137**	**144**	**119**	**91**	**157**	**157**
%of revenues	32%	32%	27%	16.1%	9.3%	8.0%	7.6%	10.6%	11.2%	9.3%	7.1%	12.4%	12.4%
Total depreciation and amortization	(322)	(296)	(286)	(293)	(297)	(319)	(314)	(303)	(305)	(307)	(296)	(225)	(178)
Adjusted operating profit	**250**	**263**	**163**	**(56)**	**(169)**	**(212)**	**(215)**	**(166)**	**(161)**	**(188)**	**(205)**	**(68)**	**(20)**
%of revenues	14.1%	15.1%	9.9%	(3.8%)	(12.3%)	(15.8%)	(16.4%)	(12.8%)	(12.5%)	(14.6%)	(16.2%)	(5.4%)	(1.6%)
Tax income (expenses)	-	-	-	-	-	-	-	-	-	-	-	-	-
Tax rate					0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
CAPEX					(298)	(301)	(241)	(231)	(283)	(278)	(259)	(178)	(178)
%of revenues					(21.7%)	(22.4%)	(18.4%)	(17.8%)	(22.0%)	(21.7%)	(20.4%)	(14.0%)	(14.0%)
Positive (negative) cash flow from working capital changes					(2)	(3)	(2)	1	1	0	1	0	
Positive (negative) cash flow from broadcasting right changes					(23)	27	24	33	31	20	13	9	
Total positive (negative) cash flow from working capital and broadcasting right changes					(25)	24	22	35	32	21	14	9	
Cash flow					**(196)**	**(170)**	**(120)**	**(59)**	**(108)**	**(138)**	**(155)**	**(11)**	**(20)**
Discounting period					0.50	1.50	2.50	3.50	4.50	5.50	6.50	7.50	7.50
Discounted cash flow					**(188)**	**(150)**	**(98)**	**(44)**	**(75)**	**(88)**	**(91)**	**(6)**	**(131)**

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Multi-Channel Television Operations (Yes) - Results of Valuation

Summary of valuation

Results of valuation	NIS millions
Portion of EV attributed to Model Years	(741)
Portion of EV attributed to the representative year	(131)
Total EV	**(871)**

In summary, the enterprise value of multi-channel television operations under the above assumptions as of December 31, 2018 is NIS (871) million, while the book value as of December 31, 2018 totaled NIS 886 million. It is noted that we reviewed the Company's enterprise value under a scenario where it does not change its technological model, and the resulting value was even more negative.

Chapter 4 - Valuation

Multi-Channel Television Operations (Yes) - Fair Value

Change in value of excess acquisition costs in Bezeq's books for Yes:

Excess acquisition costs / NIS millions	Balance sheet value as of Dec. 31, 2018	Fair value
Goodwill	33	0
Customers	266	0
Brand	238	0
Tax reserve	(116)	0
Total excess acquisition costs	**422**	**0**

<u>Summary</u>

The fair value of Bezeq's excess acquisition costs for Yes totals NIS 0.

Fair value assessment of Yes's assets

According to the accounting standard for impairment testing, Yes's recoverable amount is the higher of either its value in use and its fair value. Since the value for Yes's operations is negative, we examined the fair value of its assets.

In 2018, the Company's assets totaled NIS 1,606 million. Assets are composed, among other things, of broadcasting rights, PP&E, subscriber acquisition costs, and intangible assets .

Change in PP&E asset values in Yes's books

Yes's PP&E balance as of Dec. 31, 2018 is NIS 672 million. The fair value of its PP&E assets is as follows:

PP&E / NIS millions	Balance sheet value as of Dec. 31, 2018	Fair value
Broadcasting and receiving equipment	46	21.2
Discounted installation costs	185	1.1
ULTRA boxes*	405	72.7
Sting boxes*		15.1
Other STBs		0
Office furniture and equipment	21	2.7
Improvements to leased property	15	0
Total value	**672**	**112.8**

Conclusion: The total fair value of PP&E in our valuation was NIS 113 million.

*After considering the possibility of profit above the unit cost, we concluded that the market for used STBs is very limited, and so the set price per unit was in the top part of the price range.

Multi-Channel Television Operations (Yes) - Results of Valuation

The STB item in Yes's PP&E is composed, in technological rising order, of SD boxes, MAX boxes, HD boxes, Total boxes, Quatro boxes, and Ultra boxes. Company management stated that these STBs have been customized to Yes's technology. Therefore, in considering the fair value of Yes's STBs, we found that since these are used STBs, and due to high adaptation costs, collection costs, and the technological obsolescence of most of these STBs, the boxes do not have any disposal value except for the Ultra boxes which were introduced at the end of 2017, and the Sting boxes which can be used by all operators and by individuals. For details, see Appendix B .

We examined additional PP&E items and found that they have value as used products, as shown in the table .

Summary

The fair value of Yes's PP&E as shown in the above table totals NIS 113 million.

Change in intangible asset values in Yes's books

As of Dec. 31, 2018, Yes' intangible assets totaled NIS 107 million, composed mainly of licenses and software some of which were uniquely adapted for Yes, for use in its routine operations. As such, these assets do not have any fair value as used a used product. Intangible asset balances include upgrades to the Company's storage and back-up system, which we found to be of value.

Summary

The fair value of Yes's intangible assets totals NIS 1 million.

Multi-Channel Television Operations (Yes) - Results of Valuation

Broadcasting rights

Yes's broadcast rights totaled NIS 463 million as of December 31, 2018. This asset comprises broadcast right costs net of utilized rights. Some rights cannot be sold in the secondary market due to contractual provisions arising from the structure of the agreement dictated by regulatory restrictions (due to the requirement for exclusive procurement, procurement agreements do not allow the sale of rights on the secondary market). However, the Company's management stated that its rights in original content which Yes produces may be sold at a fair value of NIS 60 million. The details of broadcasting right calculations are as follows :

Movies and series procurement

The Company's management clarified that value cannot be attributed to movies and series since broadcasting rights are non-transferable (except options to assign rights in the case of a merger with Bezeq), and so we assess Yes's fair value for its rights in movies and series to be NIS 0.

Original content which has aired

We examined the probability for sale and the recovery rate expected from the sale* of original content which have already aired according to the year in which they were created. The fair value for Yes's rights in original content which has aired is **NIS 27 million**.

Original content which has not aired

We examined the probability for sale and the recovery rate expected from the sale* of original content which has not yet aired according to its production stage (writing, filming, ready-to-air). The fair value for Yes's rights in original content which has not aired is **NIS 33 million**.

*The probability rate for recovering the full investment through the net sale .

Chapter 4 - Valuation

Multi-Channel Television Operations (Yes) - Results of Valuation

Broadcasting rights

Conclusion: Between 2016-2018, broadcasting rights net of utilized rights ranged from NIS 420 million to NIS 460 million. In this period, revenues from content sales accounted for 0.5% to 3% of broadcasting rights net of utilized rights. The fair value of broadcasting rights was estimated at NIS 60 million, accounting for 13% of the rights as of December 31, 2018. Thus, the fair value of broadcasting rights as of the valuation date was also reasonable compared to actual sales in previous years. This is true, as the valuation deals with the disposal of these assets without any plans to continue their development. Thus, we believe that consideration for these assets at a rate of 13% of their carrying amount (equivalent to 4 years of their historical inflows) is reasonable.

Multi-Channel Television Operations (Yes) - Results of Valuation

Changes to the Value of Real Estate Rights in Yes's Books

We examined the Company's rights to real estate assets in the long term, and as of December 31, 2018 they totaled NIS 84 million, as compared to liabilities of NIS 85 million. Since Yes's commercial terms are at market prices and it can sub-let them, assets and liabilities at fair value are negligible and were not included.

Summary

The fair value for Yes's rights and obligations in real estate remains at their carrying amounts.

Changes to the Value of Vehicle Leases in Yes's Books

Since the balance is outside the scope of IFRS 16, the asset's method of presentation was specified by the Company.

Multi-Channel Television Operations (Yes) - Results of Valuation

Changes to the Value of Real Estate Rights in Yes's Books

We examined the Company's rights to real estate assets in the long term, and as of December 31, 2018 they totaled NIS 84 million, as compared to liabilities of NIS 85 million. Since Yes's commercial terms are at market prices and it can sub-let them, assets and liabilities at fair value are negligible and were not included.

Summary

The fair value for Yes's rights and obligations in real estate remains at their carrying amounts.

Changes to the Value of Vehicle Leases in Yes's Books

Since the balance is outside the scope of IFRS 16, the asset's method of presentation was specified by the Company.

Multi-Channel Television Operations (Yes) - Results of Valuation

Yes's Brand

We estimate that Yes's cash flows would be even more negative if it didn't have a brand which, according to information from the Company's management, is valued as a well-established and well-loved brand. Thus, assuming Yes's continued operation under the present format (going concern), the brand has significant value included in the DCF calculation (as he value would have been lower without the brand). This brand value is due to investment in advertising (NIS 50 million / year) and content, and so the maximum brand value depends on the going concern assumption. However, GAAP require that we asses the maximum recoverable value for Yes as a whole and not the maximum value for the brand. Under these principles, the maximum value for Yes is obtained assuming that operations are discontinued and assets are sold. Under this assumption, there is no more investment in content and advertising, and the brand clearly does not have any value for Yes itself. Therefore, we checked the possibility that another market player would buy the brand.

Our examination found that telecom market players can be divided into two groups: telecom operators offering paid TV services (HOT, Cellcom, Partner), and telecom operators which do not offer paid TV services (Golan, XPhone, Rami Levy) Companies in the first group have their own brands, and so it is unlikely that the Yes brand has any value for them. For the other companies - there are no indications that they plan to enter the broadcasting market or that they can invest hundreds of millions of shekels a year in content (investments required even before any subscribers are recruited). Therefore, they, too, are unlikely to attribute any material value to the brand.

Customers

Customers recognized in Bezeq's books represent the excess of cost from Bezeq's acquisition of Yes's shares in March 2015 (i.e. - the amortization balance of customers which existed at the time).

For Yes itself, under a going concern assumption (DCF), these customers do not have any positive value, as the Company expects to continue running a loss across the forecast period and in the representative year.

Furthermore, upon inquiries with the Company's management, we found that customers cannot be transferred to a new operator as that would change the terms of the customers' contracts (the customer does not have to agree to switch to the company that bought the customers balance, should such a buyer be found, including since television products are not uniform and customer preferences may differ). Furthermore, Yes's customers have satellite STBs, and there are no other satellite-based broadcasters in Israel. Thus, transferring customers to other operators would also require technician visits and the installation of replacement STBs.

We also checked whether any value can be attributed to the list of Company customers. The Company's legal counsel stated that the list of customers cannot be sold for legal reasons. In light of the above, and since the Company operates at a loss, we do not attribute value to the Company's customers.

Multi-Channel Television Operations (Yes) - Results of Valuation

Summary of Valuation under NAV requirements

Details / NIS millions	Balance sheet value as of Dec. 31, 2018	Write-off	Disposal value	NAV
Cash and cash equivalents	80	-	80	-
Trade receivables	132	-	132	132
Other receivables	8	-	8	8
Broadcasting rights	463	(403)	60	60
Property, plant and equipment	672	(559)	113	113
Intangible assets	107	(106)	1	1
Subscriber acquisition	29	*(29)	-	-
Real estate asset usage rights	84	-	84	84
Vehicle lease usage rights	31	**(3)	28	28
Total assets	**1,606**	**(1,100)**	**506**	**425**
Bank credit	(14)	-	(14)	-
Current maturities on debentures	(8)	-	(8)	-
Trade payables	(440)	-	(440)	(440)
Other payables	(64)	-	(64)	(64)
Provisions	(19)	-	(19)	(19)
Bank loans	(7)	-	(7)	-
Other liabilities	(10)	-	(10)	(10)
Employee benefits	(4)	-	(4)	-
Real estate leasing liabilities	(86)	-	(86)	(86)
Vehicle leasing liabilities	(35)	-	(35)	(35)
Total liabilities	**(687)**	**-**	**(687)**	**(654)**
Equity	**919**		**(181)**	**(229)**
Excess of cost - goodwill for Yes recognized in Bezeq's books	33	(33)	-	-
Excess of cost - customers	266	(266)	-	-
Excess of cost - brand	238	(238)	-	-
Excess of cost - tax reserve (net of excess of cost on tax reserve for debentures(	(116)	116	-	-
Total book value as of Dec. 31, 2018	**1,340**	**(1,521)**	**(181)**	**(229)**

Under this approach ,we assessed the net disposal value of the Company's assets, according at their previously-presented fair value.

Thus, Yes's equity, as derived from the fair value of balance sheet items revalued according to IAS 36 and IFRS 15, is negative 229 million NIS.

*Outside the scope of IAS 36; presented for the sake of convenience to clarify the overall picture.
**The asset's presentation method was provided by the Company.

Chapter 4 - Valuation

Multi-Channel Television Operations (Yes) - Results of Valuation

Summary of Valuation under NAV requirements

Under this approach ,we assessed the net disposal value of the Company's assets, according at their previously-presented fair value.

Details / NIS millions	Balance sheet value as of Dec. 31, 2018	Write-off	Disposal value	NAV
Cash and cash equivalents	80	-	80	-
Trade receivables	132	-	132	132
Other receivables	8	-	8	8
Broadcasting rights	463	(403)	60	60
Property, plant and equipment	672	(559)	113	113
Intangible assets	107	(106)	1	1
Subscriber acquisition	29	*(29)	-	-
Real estate asset usage rights	84	-	84	84
Vehicle lease usage rights	31	**(3)	28	28
Total assets	**1,606**	**(1,101)**	**506**	**425**
Bank credit	(14)	-	(14)	-
Current maturities on debentures	(8)	-	(8)	-
Trade payables	(440)	-	(440)	(440)
Other payables	(64)	-	(64)	(64)
Provisions	(19)	-	(19)	(19)
Bank loans	(7)	-	(7)	-
Other liabilities	(10)	-	(10)	(10)
Employee benefits	(4)	-	(4)	-
Real estate leasing liabilities	(86)	-	(86)	(86)
Vehicle leasing liabilities	(35)	-	(35)	(35)
Total liabilities	**(687)**	**-**	**(687)**	**(654)**
Equity	**919**		**(181)**	**(229)**

Thus, Yes's equity, as derived from the fair value of balance sheet items revalued according to IAS 36 and IFRS 15, is negative 229 million NIS.

Changes in Yes's value

Changes in Yes's value over time:

Details	NIS millions	Details
Yes valuation as of Mar. 23, 2015	2,496	Fahn Kanne valuation from May 19, 2015
Yes valuation as of Dec. 31, 2015	2,620	Giza valuation from Mar. 9, 2016
% Change	5.0%	
Yes valuation as of Dec. 31, 2016	2,551	Giza valuation from Mar. 28, 2017
% Change	(2.6%)	
Yes valuation as of Jun. 30, 2017	1,947	Giza valuation from Aug. 23, 2017
% Change	(23.7%)	
Yes valuation as of Sept. 30, 2017	1,761	Giza valuation from Nov. 27, 2017
% Change	(9.6%)	
Yes valuation as of Dec. 31, 2017	1,346	Prometheus valuation from Mar. 28, 2018
% Change	(23.6%)	
Yes valuation as of Dec. 31, 2018	(229)	Prometheus valuation (NAV) from Mar. 18, 2019
% Change	(117.0%)	

*Outside the scope of IAS 36; presented for the sake of convenience to clarify the overall picture.

**The asset's presentation method was provided by the Company.

Appendices

Appendix A

WACC - Multi-Channel Television Operations (Yes)

Calculating the discounting rate for Yes' operations

Symbol	Parameter	Value	Comments
D/V	Debt to asset value ratio	0.53	*Based on the median of comparative companies (see table(*
E/V	Equity to asset value ratio	0.47	**(D/V) = 1 - (E/V)**
D/E	Debt to equity ratio	1.13	**(D/E) = (D/V) / (E/V)**
βUL	**Unleveraged beta for comparative companies**	**0.64**	*In order to estimate the beta for these operations, we reviewed a group of similar companies. There were no publicly traded companies whose operations are identical to the operations under assessment, and so we chose companies that are partially similar to said operations yet differ from each other, or order to create a mix which would optimally reflect the Company's profile. Beta is calculated on a weekly basis over a 5-year period.*
Tax	Long term tax rate for the operations	23.0%	Long term tax rate for the operations under assessment.
βL	**Leveraged beta for the operations**	**1.20**	**βL= βUL*{1+(1-Tax)*(D/E)}**
Rf	Risk-free interest rate	3.2%	*Nominal yield to long-term maturity on NIS-based government bonds, for a 15-year period, as of December 31, .2018*
MRP	Market risk premium	5.9%	*The risk premium in the Israeli market, based on Damodaran data as of .2018*
SRP	Specific risk premium	3.5%	*Premium according to Duff and Phelps data for 2018, for mid-sized enterprises.*
Re	**Cost of equity**	13.69%	**RE = Rf + βL * MRP + SRP**
Rd	**Cost of Company debt**	4.6%	*Long-term cost of debt for the operations, based on the yield to maturity as of the valuation date of Bezeq's debentures in trading*
WACC	**Weighted average cost of capital**	**8.35%**	**WACC = Re *(E/V) + Rd*(D/V)*(1-TAX)**

The above table presents the discounting rate calculated for Yes's operations as of December 31, .2018

Since we believe the risk in these operations will not decrease compared to 2017, use used an 8.5% discounting rate, similar to the rate used in the previous valuation of the Multi-Channel Television segment.

Additional information on comparative companies:

Company	Unleveraged beta	D/V
SKY PLC*	0.64	0.18
DISH NETWORK	0.65	0.53
LIBERTY GLOBAL	0.34	0.65
Median	**0.64**	**0.53**

*Data for SKY are as of September 30, 2018

Appendix B

Fair Value of STBs

Fair value of Ultra boxes

We assumed that Yes would sell its Ultra boxes at a discount as they are used and would be past-warranty upon sale. Calculation of fair value only:

Property, plant and equipment - STBs		
STB value after depreciation and warranty (USD thousands)	21,993	Note 1
Collection costs (USD thousands)	1,087	Note 2
Tech adaptation costs (USD thousands)	1,500	Note 3
Total STB value (USD thousands)	**19,406**	
USD-NIS exchange rate as of **Dec. 31, 2018**	3.75	
Total STB value (NIS thousands)	**72,773**	

Notes:

Note 1

Property, plant and equipment - STBs	
Number of Ultra boxes (thousands)	107
Cost of new Ultra box (USD)	235
Depreciation per box (USD)	29
Deduction for expected repair costs per box (USD)	0.08
Used STB price after depreciation and repairs (USD)	206
Total value of STBs before additional costs (USD thousands)	**21,993**

Depreciation was calculated for an 8-year period based on information provided by Yes. Depreciation deducted from the STB price was calculated by dividing the STB cost by the number of years of depreciation.

Repair costs were calculated as follows:

Property, plant and equipment – STBs		Symbol
STB repair rate	1%	A
Repair costs per STB (USD)	8	B
Total cost of repairs and warranty (USD)	**0.08**	**C=A*B**

The Company stated that in the first year of operating the STBs, the repair rate was only 0.6%. As a conservative estimate, we assumed that in the second year of the STBs' life, this rate would grow to 1.0%. Since Yes would sell the boxes without warranty, this amount was deducted from the future selling price.

Note 2

Property, plant and equipment – STBs	
Number of Ultra boxes installed (thousands)	84
Collection cost per unit (NIS)	50
Collection coefficient	97%
Total collection costs (NIS thousands)	4,074
USD-NIS exchange rate as of Dec. 31, 18	3.75
Total collection costs (USD thousands)	**1,087**

We assumed a collection coefficient of 97%, since there are only a few customers with more than one Ultra box.

Note 3

The Company stated that any party buying its STBs would need to adapt them before use. Yes estimated these costs at about USD 1.5 million for all the STBs.

Appendix B

Fair Value of STBs

Fair value of Sting boxes

We assumed that Yes would sell its Sting boxes at a discount as they are used and do not support Netflix. Calculation of fair value only:

Property, plant and equipment - Sting boxes		
Value of STBs before additional costs (USD thousands)	4,200	Note 1
Collection costs (USD thousands)	182	Note 2
Total STB value (USD thousands)	**4,018**	
USD-NIS exchange rate as of **Dec. 31, 2018**	3.75	
Total STB value (NIS thousands)	**15,058**	

Notes:

Note 1

Property, plant and equipment – STBs	
Number of Sting boxes (thousands)	84
Cost of new Sting box (USD)	91
Selling price (USD)	50
Total value of STBs before additional costs (USD thousands)	**4,200**

The boxes' selling price, as provided by the Company's management.

Note 2

Property, plant and equipment – STBs	
Number of Sting boxes installed (thousands)	19
Collection cost per unit (NIS)	50
Collection coefficient	72%
Total collection costs (NIS thousands)	684
USD-NIS exchange rate as of Dec. 31, 18	3.75
Total collection costs (USD thousands)	**182**

Assuming a 72% collection rate, at an average of 1.4 boxes per customer, as specified by the Company's management.

Appendix C

Book Value - Multi-Channel Television Operations

Book Value - Multi-Channel Television Operations

Details on the book value of multi-channel television operations (Yes), as of December 31, 2018, as provided by Bezeq:

Item	Value (NIS millions)
Trade receivables	132
Other receivables	5
Short term investments	3
Broadcasting rights	463
Property, plant and equipment, net	672
Intangible assets	107
Subscriber acquisition	29
Lease right asset	115
Total	**1,526**
Trade payables	(440)
Other payables, including derivatives	(33)
Deferred income, short-term	(18)
Short-term provisions	(18)
Liabilities for termination of employment, net	(10)
Current maturities on leases	(30)
Long term leasing liabilities	(91)
Total	**(640)**
Total carrying amount according to the Company's balance sheet	**886**
Excess of cost - goodwill for Yes recognized in Bezeq's books	33
Excess of cost - customers	266
Excess of cost - brand	238
Excess of cost - tax reserve (net of excess of cost on tax reserve for debentures)	(116)
Total book value as of Dec. 31, 2018	**1,308**

Bezeq The Israel Telecommunication Corporation Limited

Impairment Test of Goodwill attributable to the Cellular Telephony Segment as at December 31, 2018

March 2019

Prometheus Financial Advisory

14 Kreminitzky St., Tel Aviv 6789912 I Tel.: 03-5617801 I Fax: 03-5617765

Introduction and Limit of Liability

On December 11, 2018, Prometheus Financial Advisory Ltd ("Prometheus" or the "Firm") was requested by Danny Oz of Bezeq The Israel Telecommunication Corp. Ltd. ("Bezeq" or the "Customer" or the "Company) to conduct an impairment test of the goodwill attributable to the domestic operator ("Domestic Carrier Segment"), mobile radio-telephone ("Cellular Telephony" or "Cellular Telephony Segment") and the multichannel television ("YES") segments, for the Company's financial statements as at December 31, 2018 (the "Valuation"). The opinion is intended for the Customer's use only and presentation in the financial report. This opinion may not be used for any other purpose without the Firm's prior written consent.

Financial studies are intended to reasonably and fairly reflect a given situation at a specific time, based on known data and reference to underlying assumptions, assessments and projections, including forward-looking information (as defined in the Securities Law, 1968), the materialization of which is uncertain. Accordingly, this Valuation is valid at the date of signature only, and is based on information from the Company and/or anyone on its behalf and other sources, and may also include financial statements, estimations, projections and assessments (the "Information"). The Valuation describes the Information highlights, the analyses and the test procedures performed, but the description is not necessarily full or detailed. It should be emphasized that the Firm does not conduct any test of the Information and assumes that it is reliable. Therefore, the Valuation does not constitute verification of the correctness, completeness and accuracy of the Information and does not include an audit regarding its compliance with the accounting principles. The Firm is not responsible for the implications of the method of presentation (accounting or other) of the Information, if any. The Information is based partially on knowledge at the time of the Valuation and various assumptions and expectations regarding both the Company and many external factors, including the market condition, existing and potential competitors and the condition of the entire market. If the information is incomplete, inaccurate or unreliable, the results of the Work may change, therefore, the Firm reserves the right to update the Valuation if new information is received. However, it should be noted that nothing has been received by the Firm that could indicate that the information is unreasonable.

It is hereby declared that the Firm is not dependent on and does not have a personal interest in the Valuation, the Company and the controlling shareholders of the Company, other than the fact that the Firm receives fees for this Valuation, and that the fees are not contingent to the results of the Valuation.

The Valuation does not constitute or replace a due diligence. Moreover, the Valuation is not intended to establish a value for a specific investor and does not constitute any legal advice or opinion. For avoidance of doubt, it is clarified that this Work does not constitute an offer, recommendation or opinion regarding the feasibility of the purchase/sale of securities or execution of any kind of transaction.

Neither the Firm, nor any company which it controls, any controlling shareholder, or any officer in any of them are responsible (unless they acted maliciously) for any damage ("Damage") incurred by relying on all or part of this Valuation, whether foreseen or not. The Customer will not be entitled to receive any amount from us for Damage, whether under contract or tort, by law or otherwise, or as punitive or special compensation, or in respect of claims arising or related in another manner to this Valuation. Moreover, and without derogating from the generality of the foregoing, if we are required (in legal or other proceedings) to pay any sum to a third party with respect to performance of this Valuation, the Customer undertakes to compensate us immediately upon our first demand for any such amount that exceeds three times our fees, unless we acted maliciously.

ed that due to rounding of figures, there may be a non-material deviation when adding up/multiplying the figures presented in this Valuation.

Previous Valuations, Information Sources

Previous financial valuations conducted:

The Firm conducted impairment testing of the goodwill of Bezeq's cellular segment as at December 31, 2018. Following is a comparison of the valuation of the segment and its key parameters (this Work) as at December 31, 2018, June 30, 2018 and December 31, 2017:

Details of work	Value of operations (NIS millions)	No. of subscribers in the benchmark year	ARPU in the benchmark year	Discount rate (post-tax)	Permanent growth
Impairment test of the cellular segment as at December 31, 2017	5,403	2,918	70	9.97%	2.5%
Impairment test of cellular segment as at June 30, 2018	3,907	3,062	61	9.97%	2.5%
Impairment test of cellular segment as at December 31, 2018	2,914	2,642	69	10.3%	2.5%

Previous Works, Information Sources

The main information sources used to prepare the Valuation are as follows:

•Audited financial statements of Bezeq and the operating segments for 2014-2017 and draft financial statement as of December 31, 2018

•A multiannual projection prepared by the management

•Impairment test of the goodwill of the domestic carrier, cellular telephony and multichannel television segments as of December 31, 2016

•Impairment test of the multichannel television segment as of June 30, 2017 and September 30, 2017

•Valuation of Bezeq's holdings in YES as of March 23, 2015

•Purchase price allocation (PPA) to YES as of March 23, 2015

•Additional financial data and various clarifications forwarded to us at our request.

•Background and market material out of open information published in websites, press articles or other public sources.

•A report regarding the global wireless communications market: BAML Q3 2018 Global Wireless Matrix

•Data of the Central Bureau of Statistics and the Bank of Israel

•Capital IQ system

•Discussions and meetings with the management of the Company and the subsidiaries

Information about the Assessor

Prometheus Financial Advisory Ltd.

Prometheus is a firm involved in economic and financial consulting and provision of expert opinions, led by the Yuval Zilberstein CPA, who serves as CEO, and Eyal Szewach, who serves as managing partner. The Firm advises its customers on mergers and acquisitions (M&A) as well as significant economic projects in various market sectors.

The work was conducted by a team headed by Eyal Szewach, founding partner of the Firm and holder of a B.Sc in Electronic Engineering from The Technion and an MBA of Business Administration from Tel-Aviv University. Mr. Szewach is an expert with over 10 years experience in conducting valuations, financial statement analysis, preparation of expert opinions and

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⑩ Brief Description of the Company

General

Bezeq The Israel Telecommunication Corp. Ltd. is a public company whose shares are traded on the TASE. The company is a key provider of telecommunications services, including domestic fixed-line communications services, mobile radio-telephone (cellular telephony) services, international communications services, multichannel satellite television services, internet access and infrastructure services, maintenance and development of communication infrastructures, provision of communication services to other communications providers, and other services related to its area of operation. The Company has a substantial market share in all of its operating segments, whereas in the fixed-line communications segment, it was declared a monopoly.

The Company owns subsidiaries through which it performs its business: Pelephone Communications Ltd ("Pelephone"), D. B. S. Satellite Services (1998) Ltd. ("DBS" and/or "YES"), Bezeq International Ltd. ("Bezeq International") and Walla! Communications Ltd. ("Walla").

The Company's operations are divided into four business segments:

Domestic fixed-line communications - This segment includes mainly the activities performed by the Company as a domestic carrier, including telephony services, Internet access infrastructure services, transmission and data-communication services, and wholesale service using the Company's physical infrastructure.

Pelephone - Mobile radio-telephone (cellular telephony) - Marketing terminal equipment, installation, operation and maintenance of cellular communication equipments and systems.

Bezeq International - International telecommunications, Internet and NEP services, telecommunications activities, and internet access services (ISP)

DBS - Multichannel television (YES) - Multichannel digital satellite television broadcasting services to subscribers.

Executive Summary

❿ Methodology and Results

Valuation Methodology

The valuation of the cellular operations was conducted using the discounted cash flow method (DCF).

The projected cash flows of operations is based, inter alia, on the results in 2015-2018, the draft financial report for 2018 and the projection of the managements of the segments for 2019-2023.

Prometheus estimated, to the best of its ability, the probability of realization of different parameters, based on information presented to us and independent analysis.

Principal Assumptions

Cellular segment: Continuation of the ARPU erosion in 2019, a certain stabilization in 2020 and a moderate increase in the subsequent years were assumed. A permanent growth rate of 2.5% and a nominal post-tax discount rate of 10% were used.

Valuation Results

Cellular segment: The value of operations in the cellular segment as at December 31, 2018 is NIS 2,914 million. According to information given to us by Bezeq, the carrying amount of this segment in its books was NIS 2,149 million, therefore, there is no need for an impairment.

Sensitivity analysis with respect to the discount rate and permanent growth

Following is an analysis of the changes in value of operations in the cellular segment with respect to changes in the discount rate and permanent growth:

		Discount rate				
		8.3%	**9.3%**	**10.3%**	**11.3%**	**12.3%**
Permanent growth	**1.5%**	3,511	3,004	2,613	2,304	2,054
	2.0%	3,768	3,191	2,754	2,414	2,141
	2.5%	4,069	3,405	**2,914**	2,536	2,237
	3.0%	4,427	3,654	3,095	2,673	2,343
	3.5%	4,861	3,945	3,303	2,827	2,461

Prometheus Financial Advisory

Chapter A - Description of Bezeq's Business

⑩ Bezeq

General

Bezeq is a public company whose shares are traded on the Tel Aviv Stock Exchange. The Company is a key supplier of communications services, including domestic fixed-line communications services, mobile radio-telephone services (cellular telephony), international communications services, multichannel satellite television services, internet access and infrastructure services, maintenance and development of communication infrastructures, provision of communication services to other communications providers, and other services related to its area of operation. The Company has a substantial market share in all of its operating segments, whereas in the fixed-line communications segment, it was declared a monopoly.

Bezeq wholly owns:

- Bezeq International Ltd. (“Bezeq International”)
- Pelephone Communications Ltd. (“Pelephone”)
- DBS Satellite Services (1998) Ltd. (“YES”)
- Walla! Communications Ltd. (“Walla”)
- Bezeq Online Ltd. (“Bezeq Online”)

Exhibit 1: Bezeq Group’s holding structure

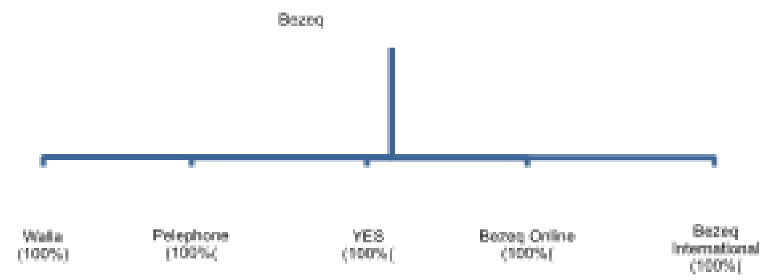
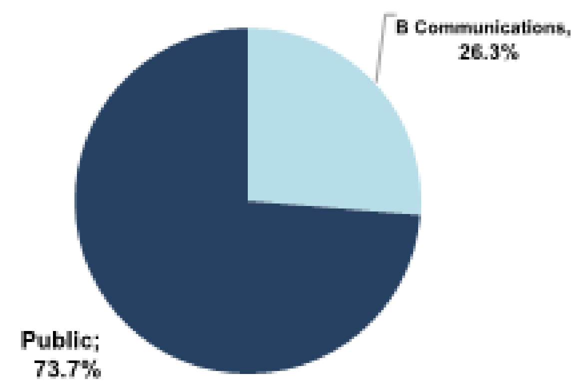


Exhibit 2: Bezeq’s ownership structure



❿ Bezeq

Exhibit 3: Development of Bezeq's market value in 2018

(NIS millions)

Bezeq's market value fell by 49% in 2018, mainly due to intensification of competition in the television segment and further loss of subscribers, the investigations in its regard, and instability in the Company's management headquarters, which will be described below.

❿ Cellular Telephony operations (Pelephone)

Pelephone

Pelephone Communications Ltd was incorporated in Israel in 1985. Pelephone engages in the provision of cellular communication services and the sale and repair of terminal equipment.

Pelephone operates under an operating license from the Ministry of Communications - a general cellular telephony license. The license is valid until 2022 with an extension option, subject to the provisions of the license, for a further six-year term, and for a further one or more six-year renewal terms.

Pelephone is one of the six mobile network operators (MNOs) on the market that own independent networks and one of the three largest well-established cellular companies in Israel. The other operators, namely Partner, Cellcom, HOT Mobile, Golan Telecom and Xfone, are its main rivals. As at the end of the first quarter of 2018, Pelephone held a 24% market share.

Pelephone generates its revenue in the following areas:

- **Basic telephone services (voice)** - A bundle of services, including voice, call completion and related services such as call waiting, follow-me, voicemail, conference calls, etc.
- **Web navigation and data communication services** - Web navigations services by 3G and 4G cellular phone.
- **Content services** - Pelephone offers its customers content services, such as data storage backup services (Pelephone Cloud), antivirus services, cyber protection services, viewing services of different television channels (Super TV) and a music library (Musix) that enables listening to a variety of music on mobile devices and PCs.
- **Roaming services** - Pelephone allows its customers to roam with their personal phones to countries worldwide and provides them with roaming coverage in over 220 countries. In addition, it provides incoming roaming services to the customers of foreign operators staying in Israel.
- **Sale of terminal equipment** - Pelephone offers different types of mobile phones, hands-free devices and related accessories that support its range of services. It also provides its customers with terminal equipment, such as tablets, laptops, modems, speakers, headphones and other related electronic products.
- **Maintenance and repair services** - Pelephone offers a repair and extended warranty service for a monthly fee which entitles the customer to repair and warranty services for their cellular phone, or for a one-time fee at the time of the repair.

⑩ Cellular Telephony operations (Pelephone)

Pelephone (contd.)

Following are main operating data about Pelephone's operations (KPIs):

Exhibit 5: Pelephone – KPIs

Pelephone's KPIs	Note	2016	2017	Q4 2018
No. of subscribers (thousands)	1	2,402	2,525	2,205
% change		(9.4%)	5.2%	(12.7%)
ARPU (NIS per month)	2	63	61	66
% change		(1.7%)	(4.4%)	8.2%

1. Unlike the trends among the well-established operators, Pelephone recruited 124,000 subscribers in 2017, mainly due to the wide deployment of sales points as part of its management's strategy to focus on growth in the subscriber listing. In 2018, Pelephone revised the definition of an active subscriber, as a result of which 426,000 prepaid subscribers were written off the subscriber listing.

2. Recently, the ARPU is declining due to increased competition following the entry of new competitors into the market (operators that own infrastructure and virtual operators), and started marketing various cellular communication bundles at low prices as part of market penetration measures. As a result of the subscriber definition change made by the Company, there was a certain increase in its ARPU.

⑩ Debt rating

Reports by rating agencies regarding Bezeq's rating

On April 30, 2018, Midroog affirmed the current Aa2.il rating for the Company's debentures (Series 6, 7, 9 and 10) with a stable outlook.

On April 26, 2018, S&P Maalot affirmed the Company's ilAA rating and downgraded the rating outlook to negative due expected further intensification of competition and in view of the instability of the Company management. On November 18, 2018, Maalot and Midroog affirmed the foregoing ratings, respectively, for the issuance of new Series 9 debentures in the amount of NIS 55 million.

⑩ Events beyond the regular course of business

Review of the events not in the ordinary course of business of Bezeq. The information is based on the Company's reports.

Investigations in terms of Bezeq Group and its controlling shareholders

On June 20, 2017, the Israel Securities Authority launched a public investigation. The investigation deals with suspicions of crimes under the Securities Law and Penal Code in respect of transactions relating to the controlling shareholder, relates to the purchase of YES shares by Bezeq from Eurocom DBS, a company that was controlled by the controlling shareholder, Shaul Elovitch. The investigation was later expanded to include transactions to provide satellite communications services between DBS and Spacecom Communications Ltd. ("Spacecom"), a company that was controlled by Mr. Elovitch, and with respect to dealings between the Ministry of Communications and Bezeq.

Senior officers in Bezeq Group were questioned as part of the investigation. At a meeting of the Company's Board of Directors held on November 15, 2017, the Board accepted Mr. Elovitch's proposal whereby until further notice he does not wish to resume the position of Chairman of the Board of Directors of Bezeq and Mr. David Granot will continue to serve as Acting Chairman of the Board of Directors. It is noted that as at the valuation date, Mr. Granot still serves as Chairman of the Board of Directors of Bezeq Group.

On November 6, 2017, the Securities Authority issued a press release regarding conclusion of the investigation and transfer of the investigation file to the Tel Aviv District Attorney's Office (Taxation and Economics). According to the notice, the ISA has concluded that there is prima facie evidence on offenses of:

1. The entitlement of the Company's controlling shareholder to payment of NIS 170 million as part of the transaction for the purchase of YES shares from the controlling shareholder, by Bezeq, payment that was contingent upon YES meetings certain targets.
2. Leaking material from the independent committee of the Company's Board of Directors that was required to examine interested party transactions (the transaction for the acquisition of YES shares by the Company and the transaction between DBS and Spacecom Ltd. for the purchase of satellite segments) to the Company's controlling shareholder and his associates.
3. Promotion of the Company's interests in the Ministry of Communications, in violation of the Penal Code and Securities Law. The notice also relates to transfer of the investigation file to the District Attorney's Office and that the District Attorney's Office is authorized to decide on the continued handling of the case.

On February 28, 2018, Bezeq's Board of Directors announced its resolution to appoint the head of the Company's Business Division, Kobi Paz, Acting CEO of Bezeq.

❿ Events beyond the regular course of business

Debt settlement in Eurocom Group and replacement of control in Bezeq

On April 22, 2018, a liquidation order was issued for Eurocom Communications (which entered into force on May 3, 2018), where in as part of the liquidation decision the Court clarified that its ruling does not derogate from the control permit regarding the Company. Subsequently, on October 24, 2018, the Company received notice from Internet Gold-Golden Lines Ltd. ("Internet Gold"), which is controlled by Eurocom Communications and controls B Communications, the controlling shareholder in the Company, that the special managers of Eurocom Communications who were appointed in Eurocom's liquidation process, were confirmed as the holders of the control permit (effective from May 3, 2018), pursuant to Section 4D of the Communications Law and Section 3 of the Communications Order.

On January 16, 2019, Internet Gold declared insolvency and cessation of payments to debenture holders. On February 4, 2019, Internet Gold and the representative of the Company's debenture holders announced the Company's intention to look for a buyer for B Communications shares. Moreover, the Ministry of Communications allowed Internet Gold to reduce its rate of holdings in B Communications to 35% (from 50%) without derogating from its definition as an Israeli company.

❿ Events beyond the regular course of business

After Eurocom DBS failed to respond to the demand, on January 31, 2018, Bezeq motioned the Tel Aviv District Court for a liquidation order for Eurocom DBS on grounds that Eurocom DBS is insolvent.

On February 23, 2018, Eurocom Group filed motioned the court for approval of an arrangement with its creditors. The motion to approve the arrangement was filed after the meeting of Eurocom creditors approved the arrangement. As part of the arrangement, Messrs. Naty Saidoff and Tamir Cohen (who submitted the proposal) would invest significant equity in return for the option of controlling Eurocom, through the entity Shayma Investments S.A., a company controlled by them. In addition to their above proposal, others (including Discount Investments) also made proposals to Eurocom's creditors. The other proposals were not accepted or were shelved. Conclusion of the arrangement depends on the following terms:

1. Obtaining the approval of the court for the arrangement, including possible adjustments to the arrangement that might be necessary according to its decision.
2. Receiving a pre-ruling from the tax authorities regarding different aspects of the arrangement.
3. Terms relating to impairment events or material changes.
4. Obtaining any regulatory approval required by law (including a permit to control Bezeq by the investors, which is required for exercising the options, etc.).

Accordingly, at the option exercise date (subject to approval of the arrangement and fulfillment of the foregoing conditions), Eurocom's holding structure did not change. According to the proposed arrangement, even if the arrangement is approved, the preconditions are met and the option is exercised, Eurocom will continue to control Bezeq. However, the arrangement permits reviewing the option of a direct purchase of the Group's assets by the investors, subject to all the tests and approvals required by law.

On February 25, 2018, B Communications Ltd., the indirect controlling shareholder of the Company, sent a letter to Bezeq to convene an urgent Board meeting to discuss the composition of the Company's Board of Directors and raise a proposal to appoint three new directors to the Company's Board (Shlomo Rodav, Doron Turgeman and Tamir Cohen), in parallel and subject to the directors Shaul, Or and Orna Elovitch ceasing their tenure on the Company's Board.

In conclusion, the investigations in respect of the Company and the managerial instability impact Bezeq's operations in several channels:

- Negative pressure on Bezeq's share.
- Management of the Company.
- Decreased chance for significant regulatory relief in the upcoming years.

Chapter B - Communications Market

⑩ Communications market in Israel

General

The communications market is divided into six main sub-markets:

1. Cellular telephony
2. Fixed-line telephony (including interconnection through the internet - VOB/VOIP)
3. Multichannel television (satellite/cable/IPTV)
4. Internet service provider (ISP)
5. International services (ILD)
6. Broadband infrastructures (ADSL/cable/fiber)

The global communications market in general and Israeli market in particular, is characterized by rapid development and frequent changes in terms of technology and regulation. Whereas in the past competition in the communications market focused on the independent communications providers in each operating segment separately, in recent years, there is a trend of merging of communications groups that operate in several segments simultaneously, utilizing business synergies, subject to regulatory restrictions in the industry.

The recent regulatory changes enabled the entry of additional and relatively small participants, such as virtual operators and companies that own independent infrastructure (partial) in the cellular segment.

Moreover, technological and strategic changes in the television segment enabled the entry of IPTV operators and streaming services. To date, the four major communications groups, Bezeq, HOT, Cellcom and Partner, operate in all market segments:

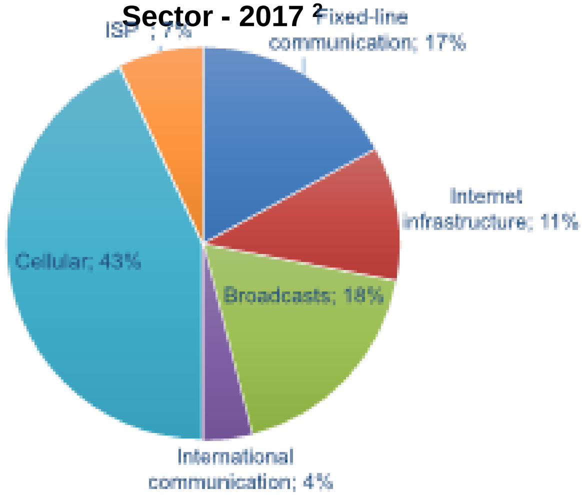
	Bezeq	Cellcom	Partner	Altice
Fixed-line telephony	Yes	Yes	Yes	Yes
Internet services	Yes (Bezeq + Bezeq International)	Yes	Yes	Yes
Television	Yes (through YES)	Yes	Yes	Yes
ILD	Yes	Yes (Netvision)	Yes	Yes
Mobile	Yes (Pelephone)	Yes	Yes	Yes (HOT Mobile)

In 2017, the communications market revenue amounted to NIS 19.2 billion[1], a decrease of 5.5% compared to 2016, mainly due to increased competition and reduced prices in all segments.

1. According to Ministry of Communications data.

❿Communications market in Israel

Exhibit 7: Breakdown of Revenue in the Communications Sector - 2017 [2]



Main Communications Companies

Bezeq

Bezeq is active in all market segments. It was declared a monopoly by the Antitrust Commissioner, inter alia, in the telephony infrastructure and high-speed Internet segments.

Bezeq is the sole communications group that holds a significant market share in one of the sub-markets and it is therefore obligated to have full structural separation between all of the different services that it provides.

2. *Source: Public information published by the Ministry of Communications*

HOT

As with Bezeq, HOT is also active in all segments of the market and the structural separation obligation applies to it in the cellular and ISP segments. Unlike Bezeq, the obligation to unbundle the service bundles offered by HOT applies only between the cellular or ISP services and the other services. Therefore, it can offer a triple bundle that includes telephony, internet infrastructure and television services.

Cellcom

Cellcom is a communications service provider that offers its customers mainly cellular services, fixed-line telephony, international telephone, ISP and related services, and since December 2014, television services over the Internet as well. As at the valuation date, among Cellcom's offers is a Quarttro bundle that includes television, fixed-line telephony, cellular and internet.

Partner

Partner offers cellular services, fixed-line telephony, international telephone, ISP and related services. In June 2017, Partner started offering OTT television services under the Partner TV brand, thereby becoming the fourth communications group to operate in all market segments.

⑩ Communications market in Israel – Cellular

Cellular Market - General

Cellular communications operates through two main elements - mobile phones and fixed broadcasting facilities. The mobile phone transmits radio waves to the antenna installations of the broadcasting facilities, which receive the radio waves from them. The cellular technologies used to date in Israel until now are known as GSM/CDMA (2G), UMTS (3G) and LTE (4G). There is currently a trend of lateral adoption of 4G technology, due to the increasing demand for data traffic by the consumers.

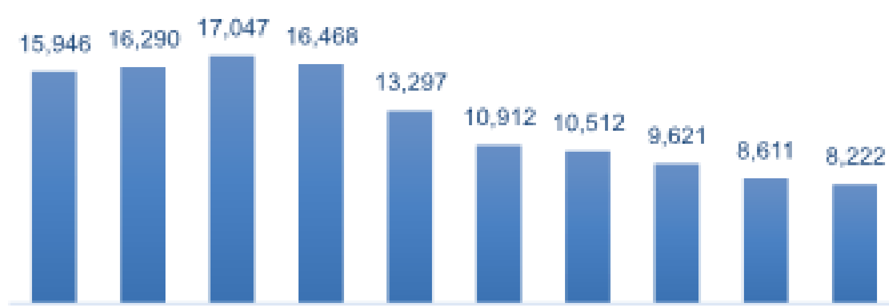
Until 2012, four independent operators (MNOs) operated in the cellular market: Pelephone, Cellcom, Partner and Mirs (now HOT Mobile). As opposed to the first three operators, until 2012 Mirs operated on the Integrated Digital Enhanced Network (IDEN), which was used mainly by public entities such as the IDF and companies that demonstrated a need for such service. As part of the regulatory measures taken by the Ministry of Communications to intensify competition in the cellular market, in 2012 new operators entered the market:

1. **Operators that own infrastructure:** Golan Telecom and HOT Mobile (which was acquired by HOT Group for integration in the traditional cellular market).
2. **Virtual operators:** Operators such as Rami Levy Communications, Telser, U-Phone, Home Cellular, etc. To date, many of the virtual operators were acquired by the MNOs.

Entry of new operators led to an increase in churn rate at the well-established companies and an ongoing price war, which together resulted in erosion of profits of the well-established cellular companies.

There are currently six operators in Israel that hold a full license granting them the right to operate cellular antennas: Pelephone, Cellcom, Partner, HOT Mobile, Golan Telecom and Marathon 018.

Exhibit 13: Revenue in the cellular market 2008-2017 (in NIS millions)[7]



The revenue in the cellular market has declined from a peak level of NIS 17 billion in 2010 to NIS 8.2 billion in 2017, despite the increase in number of subscribers.

7. Source: Public reports of the Ministry of Communications regarding revenue in the cellular market.

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Communications market in Israel – Cellular

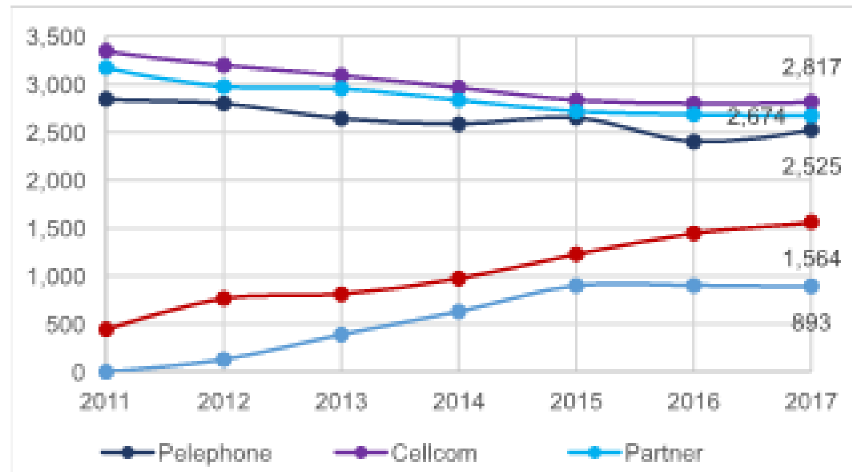
Business Environment and Competition

In 2011, the Ministry of Communications held a frequencies tender aimed at adding two new operators to the industry. In April 2011, HOT Mobile and Golan Telecom were announced the winners of the tender. After winning the tender, the new operators signed domestic roaming agreements with the well-established operators as an interim solution until completion of deployment of their independent network. As part of the market penetration measures, the new operators offers bundles that include web navigation, calls and SMS at a fixed monthly price (unlimited bundles). Opening the market to competition led to decreased prices and increased customer portability, resulting in ongoing impairment of the results of the well-established operators.

Other than the new cellular operators, virtual operators were added to the market, whose impact is less.

Subscribers and ARPU

Exhibit 14: Subscriber listings - Operators that own infrastructure[8]

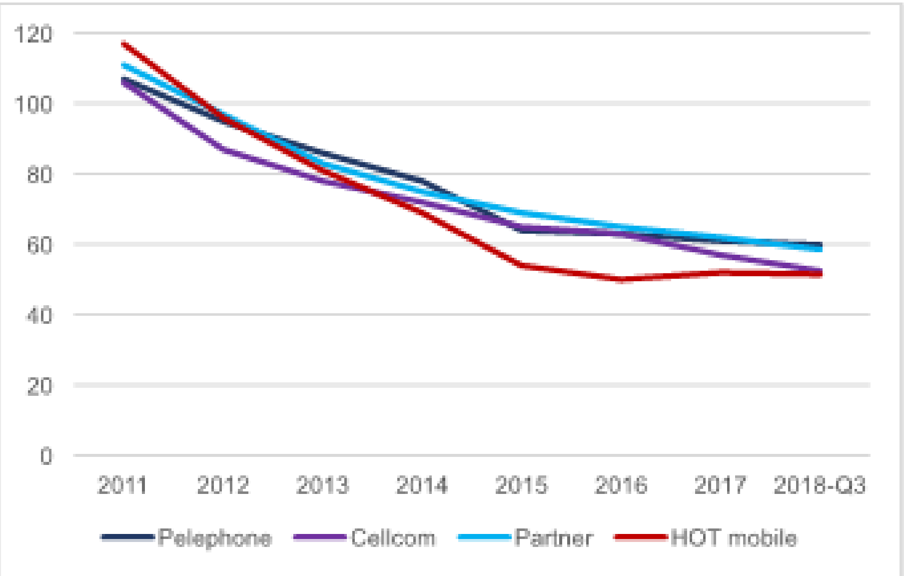


As shown in the above chart, the number of subscribers of the well-established operators is continuously decreasing over the years, whereas the new operators, HOT Mobile and Golan Telecom, demonstrate a year to year increase, emphasizing the intensifying competition in the cellular market in Israel and the challenges faced by the well-established operators. Unlike the other well-established operators, Pelephone succeeded in producing a positive net recruitment in 2016 and 2017.

8. *Source: The Company's financial statements.*

⓾ Communications market in Israel – Cellular

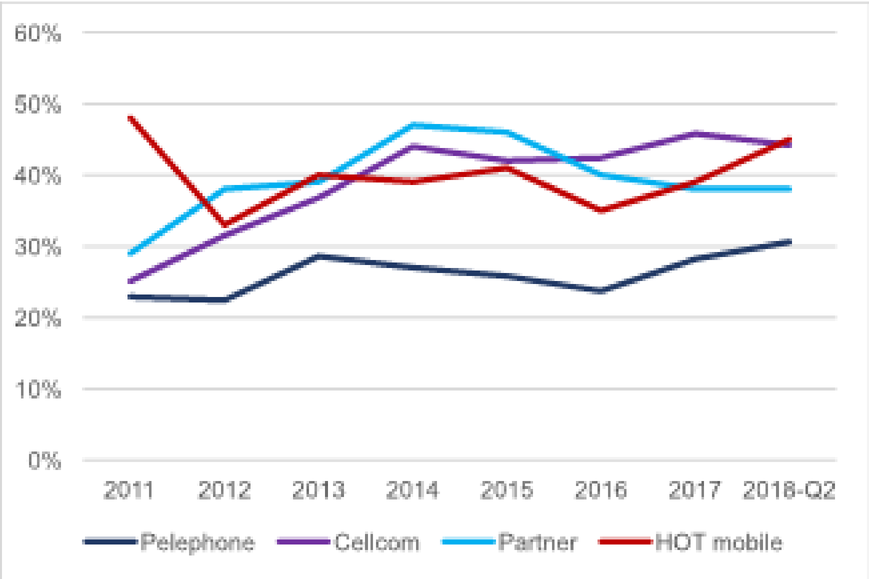
Exhibit 15: ARPU of the operators that own infrastructure (excluding Golan Telecom)[9]



The above chart shows that the average monthly revenue per user (ARPU) in constantly decreasing. E.g., the ARPU of the well-established operators has eroded by 50%, from a level of NIS 106-NIS 111 in 2011 to NIS 60-53 in 2018. In the last two years, the erosion rate abated at all operators.

9. *Source: The Company's financial statements.*

Exhibit 16: Churn rates[10]



The churn rate of the MNOs rose with opening of the market to competition and facilitation of consumer portability. On the other hand, Pelephone succeeded in maintaining a lower churn rate than the other operators.

10. *Source: The Company's financial statements.*

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⑩ Communications market in Israel – Cellular

Recent developments

Network sharing

In view of the competition in the cellular market and the ARPU erosion, certain entities in the market signed network sharing agreements - joint cellular network maintenance and development, in order to save costs. Following is a review of the existing agreements at the date of the valuation.

- HOT Mobile – Partner: In November 2013, Partner and HOT Mobile announced signing of an agreement to establish a partnership to maintain, develop and operate a single advanced cellular network for both companies, each of which will hold half of the rights thereof. According to the report, each of the parties will continue to hold and operate their core network separately and provide cellular communications services to their customers only. In April 2015, both companies announced that the Ministry of Communications officially approved the agreement.
- Golan Telecom – Cellcom: On January 3, 2017, collaboration between Cellcom and Golan Telecom was reported, with the aim of joint development of networks and technologies. The agreement received regulatory approval in March 2017.
- Xfone - Cellcom: In March 20, 2017, the Ministry of Communications approved an agreement between Cellcom and 018 Xfone Ltd. ("Xfone") for sharing of Cellcom's 4G network and provision of hosting services on the 2G and 3G networks.
- Migration of Cellcom, Golan Telecom and Xfone to a shared network: In March 19, 2018, the Ministry of Communications approved an agreement between Cellcom, Golan telecom and Xfone to establish an infrastructure operation company owned equally by these companies. The company is responsible for operating a 3G network, and operation and deployment of a 4G network for the operators.

Golan Telecom - Electra Transaction

- On January 3, 2017, Electra Consumer Products Ltd. ("Electra") reported the acquisition of 100% of Golan Telecom in return for NIS 350 million. On April 5, 2017, following approval of the transaction by the Antitrust Commission and the Ministry of Communications, the transaction was concluded.

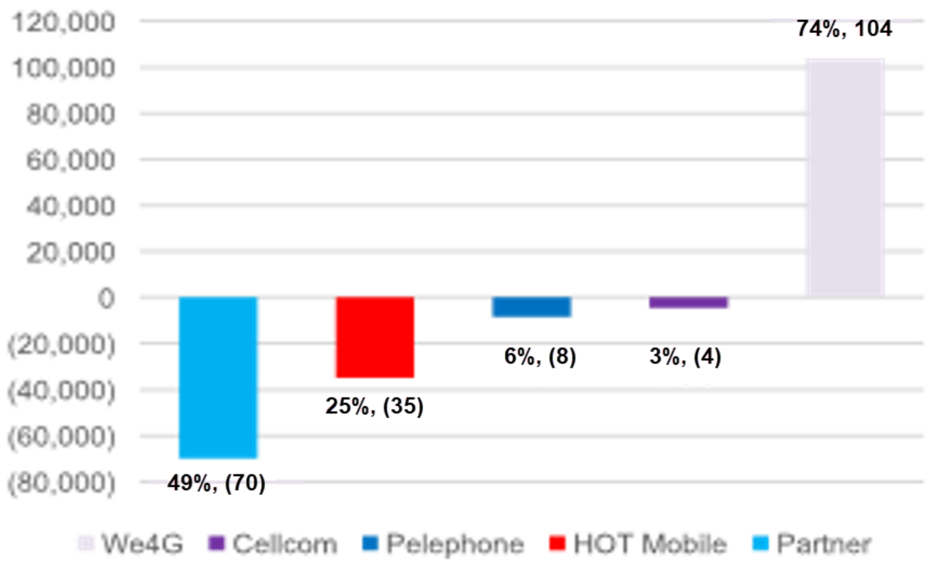
Elimination of purchase tax on cellular phones

In April 2017, the Finance Minister announced an economic plan that includes, inter alia, the elimination of import duties and purchase taxes. As part of this plan, the Finance Ministry decided to abolish purchase tax on imported cellular devices, which had been 15% of the value of the device. Pursuant to this move, there are two opposing effects on the performance of the cellular companies that sell terminal equipment, namely a decrease in revenue from terminal devices due to reduced prices and an increase in profits due to growth in demand.

⑩ Communications market in Israel – Cellular

Entry of Xfone into the market

Exhibit 18: Subscriber portability from entry of Xfone until January 2019 (in thousands)[11]



On April 10, 2018, Xfone launched the activity of its We4G cellular brand by marketing a lifelong 40GB deal at NIS 29. The competitive pricing led to erosion of the subscriber listing of the well-established operators, mainly Partner and HOT Mobile.

11. Data from the subscriber portability system, according to Globes.

⑩ Communications market in Israel – Cellular

Exhibit 17: EBITDA rates from <u>services</u> in select countries in Q3, 2018[12]

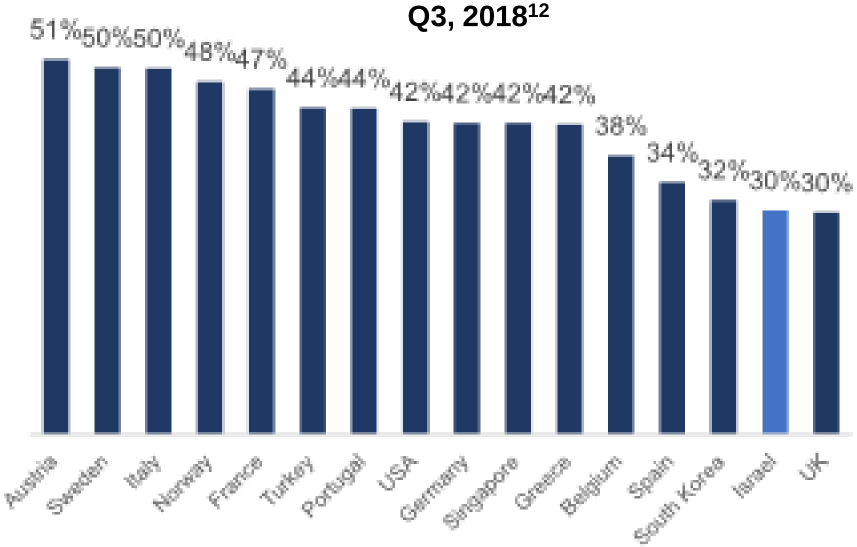
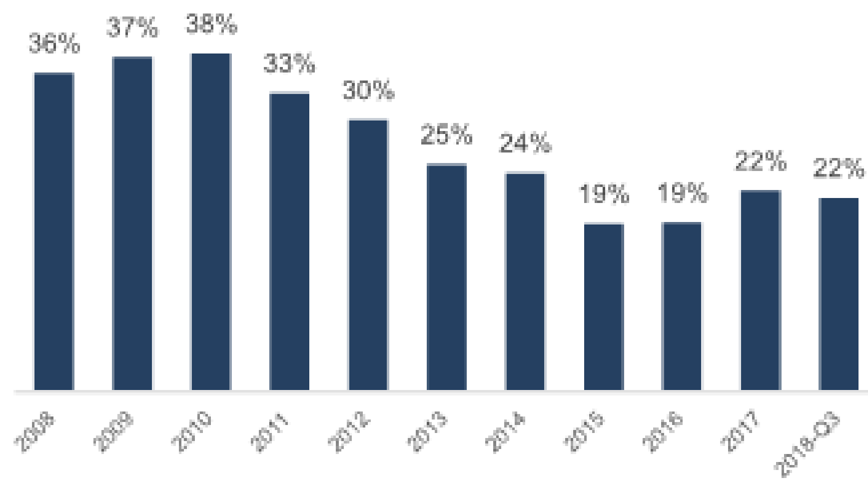


Exhibit 18: Average EBITDA rate of the well-established operators in Israel[13]



Exhibits 17-18 shows that the EBITDA rate from cellular services is higher in most developed countries than in Israel, due to the fierce competition in this market in recent years. The total EBITDA rate of the well-established operators dropped between 2011-2015 and is rising moderately in recent years. Notably, this increase is mostly due to early adoption of the IFRS15. Without this effect, the EBITDA rate of the well-established operators would probably not have changed materially in recent years.

12. *Source: Merrill Lynch Global Wireless Matrix Q3 2018*

13. *Source: Financial statements of Bezeq, Cellcom and Partner.*

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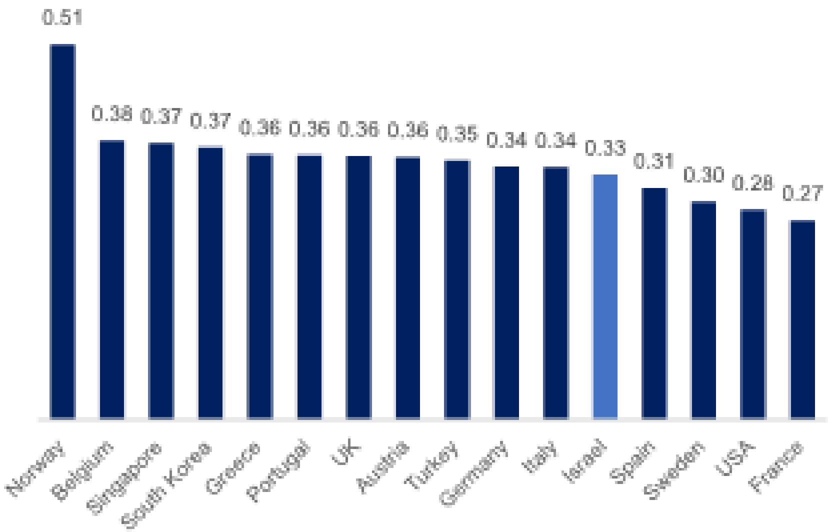
⑩ Communications market in Israel – Cellular

Exhibit 19: HHI in Select Countries, in Q3 2018[14]



The Herfindahl-Hirschman Index is a market concentration measure and the accepted indicator of the market concentration in a sector. As shown in the above flow chart, the market concentration in Israel is relatively low according to this index, although there are more competitive countries.

Cellular Market – Conclusion

The cellular segment is highly competitive in recent years. This competition leads to a decline in revenue as well as higher churn and portability rates than usual before the reform in this market.

In the last two years, a moderation in the ARPU erosion rate is evident, mainly due to a decrease in consumer sensitivity to price, and the acquistion of Golan Telecom by Electra.

In our estimation and that of entities in this market, the current ARPR levels are not economically feasible and it is reasonable to assume that in the coming years there will be multiple moderate increases or minimal sharp increases in the monthly ARPU.

14. *Source: Merrill Lynch Global Wireless Matrix Q3 2018*

Chapter C - Analysis of Financial Statements

⑩ Balance Sheet - Cellular Operations

Statements of Financial Position of Pelephone for December 31, 2015-2017 (audited data) and December 31, 2018 (draft financial statements):

NIS million	December 31, 2015	December 31, 2016	December 31, 2017	December 31, 2018
Assets	**Audited**	**Audited**	**Audited**	**Draft**
Current assets	1,420	1,275	1,128	913
Non-current assets	1,854	2,019	2,143	3,211
Total assets	**3,274**	**3,294**	**3,271**	**4,124**
Liabilities + capital				
Current liabilities	448	465	442	619
Non-current liabilities	70	104	94	806
Equity	2,756	2,725	2,735	2,699
Liabilities + capital	**3,274**	**3,294**	**3,271**	**4,124**

Analysis of Main Items

Assets

Current assets: The assets of the operations continued to decrease in 2018, mainly due to a decline in revenue expressed in a reduction in trade receivables and trade payables

Property, plant and equipment: An ongoing decline in property, plant and equipment as a result of high depreciation expenses from current investments.

Long-term interested party loan: A loan given to Bezeq.

Right of use of leased assets: An increase in the item resulting from application of IFRS 16 for the first time.

Liabilities

Financial liabilities: As at December 31, 2018, Pelephone's operations do not have financial liabilities, other than employee retirement benefits.

⑩ Profit and loss - Cellular operations

Pelephone's Statements of Income for 2015-2017 (audited data) and 2018 (draft financial statements):

NIS million	2015 Audited	2016 Audited	2017 Audited	2018 Draft
Revenues from services	1,999	1,819	1,782	1,755
Change vs the parallel period		(9.0%)	(2.0%)	(1.5%)
Revenues from sales of terminal equipment	891	812	763	688
Change vs the parallel period		(8.9%)	(5.9%)	(9.9%)
Total Revenues	**2,890**	**2,630**	**2,546**	**2,443**
Change vs the parallel period		**(9.0%)**	**(3.2%)**	**(4.0%)**
Payroll	381	378	384	379
% of revenue	13.2%	14.4%	15.1%	15.5%
General and operating expenses (including payments for leases)	1,933	1,840	1,707	1,669
% of revenue	66.8%	69.9%	67.0%	68.3%
Amortization and depreciation	418	380	383	402
% of revenue	14.5%	14.5%	15.1%	16.3%
Total operating expenses	**2,733**	**2,598**	**2,474**	**2,450**
% of revenue	**94.5%**	**98.8%**	**97.5%**	**100.3%**
Operating profit	**157**	**32**	**72**	**(7)***
% of revenue	**5.4%**	**1.2%**	**2.8%**	**(0.3%)**
Adjusted EBITDA	**576**	**412**	**455**	**395**
% of revenue	**19.9%**	**15.7%**	**17.9%**	**16.2%**
CAPEX	426	241	308	306
% of revenue	14.7%	9.2%	12.1%	12.5%
Adjusted EBITDA minus CAPEX	**150**	**171**	**146**	**89**
% of revenue	**5.2%**	**6.5%**	**5.8%**	**3.6%**

* In the Company's signed financial statements as at December 31, 2018, the operating profit was NIS (2) million. The difference is due to the fact that the above report includes payments for leases.

Analysis of Main Items

Revenue

- Revenue from cellular services: Pelephone's revenue from cellular services continued to decrease in 2018, although moderately due to growth of the subscriber listing that was offset by continued erosion of the ARPU. The revenue from services in 2018 was NIS 1,755 million, a downturn of 1.5% compared to revenue in 2017 of NIS 1,782 million.
- Revenues from sales of terminal equipment: The revenue from the sale of terminal equipment fell in 2018 by 9.9%, mainly due to a decrease in sales and launching of relatively weak devices.

In conclusion, the revenue of the cellular operations in 2018 was NIS 2,443 million, a decline of 4.0% compared to NIS 2,545 million in 2017.

⑩Profit and loss - Cellular operations

Expenses, EBITDA, CAPEX, and operating cash flows

Pelephone's **expenses** decreased by NIS 30 million (1%) in 2018 compared to 2017, but their percentage out of the total revenue rose.

The EBITDA rate eroded in 2018 by 1.7% compared to the EDIBTA rate in 2018, and Pelephone recognized an **adjusted operating profit** of NIS 7 million.

In terms of operating cash flows (before working capital changes and tax expenses), erosion was measured, as expressed in the adjusted EBITDA minus CAPEX, when the rate declined by 2.2% in 2018 compared to 2017, mainly due to the above revenue decrease.

In conclusion, in 2018 erosion of Pelephone's profits was measured to the point of an operating loss, mainly in view of the imbalance in the market.

⑩ June 2018 projection compared to actual results - Cellular operations

Projection compared to performance - 2018 (NIS millions)	Projection*	Actual	Difference
Revenues from services	1,760	1,755	(5)
Sale of terminal equipment	753	688	(65)
Total revenue	**2,513**	**2,443**	**(70)**
Total operating expenses	2,504	2,450	(54)
% of revenue	99.64%	100.3%	
Operating profit	**9**	**(7)**	**(16)**
% of revenue	0.36%	(0.3%)	
Amortization and depreciation	401	402	1
Adjusted EBITDA	**410**	**395**	**(15)**
% of revenue	16.32%	16.16%	
Investments (CAPEX)	312	306	(6)
% of revenue	12.42%	12.53%	
EBITDA - CAPEX	**98**	**88**	**(10)**
% of revenue	3.90%	3.62%	

* According to the projection of Pelephone's management that was used for the valuation as at June 30, 2018.

The Company's projection for the cellular operations prepared in mid-2018 is presented on the left against the actual expenses, which are based on known data of the first three quarters of 2018 and the draft financial statements for the fourth quarter 2018.

Revenue: The revenue of the operations was NIS 70 million lower than the Company's projection for 2018, mainly due to a negative deviation in the revenue from terminal equipment sales.

- **Expenses, EBITDA, CAPEX, and operating cash flows: Expenses** of the operations were NIS 54 million lower than the Company's budget, mainly due to a decrease in the cost of sale of terminal equipment in line with a decline in revenue. The adjusted **EBITDA** in 2018 was NIS 15 million lower than expected that year. In terms of operating cash flows (before changes in working capital and tax expenses), as expressed in EBITDA less CAPEX, a difference of NIS 10 million was measured compared to the Company's projection.

In conclusion, there was no material difference between the June 2018 projection and the actual results.

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Chapter D - Valuation

❿Valuation Methodology

Subscriber listing base

The revenue from Pelephone's prepaid subscribers is not material compared to its total revenue. Pelephone's management decided to revise the definition of an active subscriber so as not to include IoT subscribers, and to add separate reference to prepaid subscribers, according to which a prepaid subscriber will be included in the active subscriber listing as from the date at which loading is executed, and will be derecognized from the active subscriber listing if no outgoing use is made for six months.

The change entered into force at the beginning of the third quarter of 2018 and as a result, 426,000 prepaid subscribers are were derecognized from Pelephone's active subscriber listings. Such subscriber derecognation led to an increase in ARPU of NIS 11.

This derecognition did not affect Pelephone's revenue and cash flows or the assumptions and results of this valuation.

Revenue

Revenues from services

Subscribers

Recently, the well-established cellular operators are characterized by a loss of subscribers compared to Pelephone, that demonstrated a growth in subscriber listings in the last two years, mainly due to successful implementation of its growth strategy that included, among other things, wide deployment of sales points.

In 2019, we adopted the Company's projection regarding a positive cumulative recruitment of 127,000 subscribers. In 2020-2023, a positive cumulative recruitment of 310,000 subscribers, mostly postpaid, was assumed. Notably, the subscriber listing growth in 2020-2023 is based on the Company's projection in view of the accuracy of its projections in the previous year and an update of the projections in view of the market condition. In conclusion, the total subscriber listing will grow from 2,205,000 subscribers at the end of 2018 to 2,642,000 at the end of 2023.

ARPU

It was assumed that the current level of prices is not sustainable in the long term. The number of operators in the Israeli cellular market is relatively high for the size of the area and quantity of users in Israel. It is reasonable that in the long term, prices will increase to an economically feasible and sustainable level. Continuation of the ARPU erosion in 2019, a certain stabilization in 2020 and a moderate increase in the subsequent years were assumed.

As a result of these assumptions, the total revenue from services will grow from NIS 1,755 million in 2018 to NIS 2,153 million in 2023, a compound annual growth rate (CAGR) of 4.2%.

❿Cellular segment - Key assumptions - KPIs in the Cellular services

Projected KPIs

Year	Q4A 2018	2019E	2020E	2021E	2022E	2023E
Subscribers (thousands)						
Subscribers, end of period	**2,205**	**2,332**	**2,427**	**2,502**	**2,572**	**2,642**
% change	**0.9%**	**5.8%**	**4.1%**	**3.1%**	**2.8%**	**2.7%**
ARPU (NIS)						
Weighted ARPU	**66**	**64**	**64**	**66**	**68**	**69**
% change	**(2.8%)**	**(3.5%)**	**0.4%**	**2.6%**	**2.3%**	**1.8%**

Note:

The weighted ARPU includes revenue for terminal equipment services, according to Pelephone's measurement method.

Revenues from sales of terminal equipment:

It was assumed that in 2019, the total revenue from the equipment sales will be NIS 6 million lower than in 2018 and amount to NIS 682 million (price and quantity effect). From 2019 onwards, a further erosion at a fixed rate of 1.2% annually until 2023 was assumed. Notable, these assumptions are based on the projection of Pelephone's management.

Revenue - conclusion

Year	2018A	2019E	2020E	2021E	2022E	2023E
Revenue from the sale of terminal equipment	688	682	675	666	658	650
Revenues from services	1,755	1,752	1,838	1,954	2,058	2,152
Total revenue (NIS million)	**2,443**	**2,434**	**2,513**	**2,620**	**2,716**	**2,802**
% change	(4.0%)	(0.3%)	3.2%	4.3%	3.7%	3.2%

When combining the above assumptions, Pelephone's total revenue will grow from NIS 2,443 million in 2017 to NIS 2,802 million in 2023.

❿Cellular segment - Key assumptions

Operating expenses (NIS millions)

Projected operating expenses of the cellular operations in 2019-2023:

Year (NIS millions)	2018A	2019E	2020E	2021E	2022E	2023E
Payroll expenses:	379	372	361	343	344	350
% of Revenues	15.8%	15.3%	14.4%	13.1%	12.7%	12.5%
General and operating expenses*	1,410	1,450	1,453	1,456	1,423	1,427
% of Revenues	57.34%	59.6%	57.8%	55.6%	52.4%	50.9%
Payments for leases	259	254	255	255	255	255
% of Revenues	10.6%	10.4%	10.1%	9.7%	9.4%	9.1%
Total operating expenses (adjusted)	**2,048**	**2,076**	**2,069**	**2,054**	**2,022**	**2,032**
% of Revenues	83.8%	85.3%	82.4%	78.4%	74.5%	72.5%

* Including other income (expenses), net

The decrease in expenses is due mainly as a result of the restructuring plan. The projected expenses assumed by us are different to the Company's projection in terms of implementation of the restructuring plan; whereas we assumed that the Company will implement the plan partially, the Company believes that it will be exercised in full.

❿ Cellular segment - Key assumptions

EBITDA (adjusted)

When combining the above assumptions regarding the operating revenue and expenses, it was assumed that the adjusted EBITDA will grow from NIS 395 million in 2018 (16.2% of the revenue) to NIS 771 million in 2023 (27.5% of the revenue).

NIS million	2015A	2016A	2017A	2018A	2019E	2020E	2021E	2022E	2023E
Adjusted EBITDA	**576**	**412**	**455**	**395**	**358**	**443**	**566**	**694**	**771**
% of revenue	19.9%	15.7%	17.9%	16.2%	14.7%	17.6%	21.6%	25.5%	27.5%

Tax expenses

A corporate tax rate of 23% was assumed based on the current statutory tax rate in Israel.

CAPEX

The projected CAPEX is in line with Pelephone's projection. In the terminal year, we estimated an investment level of 14% of the turnover, and likewise for the CAPEX level in 2022.

Working capital

The changes in working capital of the operations are based on the average working capital as a percentage of the revenue in the last three years.

⑩Cellular segment - Key assumptions

Discount rate

The discount rate used in this valuation is 10.3% (equivalent to 12.2% before tax), according to the CAPM model (for further information, see Appendix A).

Permanent growth

Since prices hikes are expected in this market in the long term, a natural increase in the number of subscribers and development of new revenue channels, such as the Internet of Things (IoT), it was assumed that the permanent growth will be 2.5%, the same as that used in the valuation of operations as at December 31, 2017 and June 30, 2018.

⑩ Cellular segment - Projected cash flows

NIS million	2018A	2019E	2020E	2021E	2022E	2023E	TY
Revenues from services	1,755	1,752	1,838	1,954	2,058	2,153	
Sale of terminal equipment	688	682	675	666	658	650	
Total revenue	**2,443**	**2,434**	**2,513**	**2,620**	**2,716**	**2,802**	**2,872**
% change compared to parallel period	(4.0%)	(0.4%)	3.2%	4.3%	3.7%	3.2%	2.5%
Payroll expenses	(379)	(372)	(361)	(343)	(344)	(350)	
% of revenue	15.5%	15.3%	14.4%	13.1%	12.7%	12.5%	
General and operating expenses*	(1,410)	(1,450)	(1,453)	(1,456)	(1,423)	(1,427)	
% of revenue	57.3%	59.6%	57.8%	55.6%	52.4%	50.9%	
Payments for leases	(259)	(254)	(255)	(255)	(255)	(255)	
% of revenue	10.6%	10.4%	10.1%	9.7%	9.4%	9.1%	
Total operating expenses (net of amortization and depreciation)	**(2,048)**	**(2,076)**	**(2,069)**	**(2,054)**	**(2,022)**	**(2,032)**	
% of revenue	83.8%	85.3%	82.4%	78.4%	74.5%	72.5%	
Adjusted EBITDA	**395**	**358**	**443**	**566**	**694**	**771**	**790**
% of revenue	16.2%	14.7%	17.6%	21.6%	25.5%	27.5%	27.5%
Total amortization and depreciation	(402)	(384)	(384)	(378)	(384)	(411)	(411)
Adjusted operating profit	**(7)**	**(26)**	**60**	**188**	**309**	**360**	**379**
% of revenue	(0.3%)	(1.1%)	2.4%	7.2%	11.4%	12.8%	13.2%
Tax revenues (expenses)		-	(8)	(43)	(71)	(83)	(87)
Tax rate		0%	13%	23%	23%	23%	23%
CAPEX	(306)	(374)	(371)	(388)	(407)	(401)	(411)
% of revenue	(12.5%)	(15.3%)	(14.8%)	(14.8%)	(15.0%)	(14.3%)	(14.3%)
Positive (negative) cash flows from changes in working capital		(3)	1	1	1	1	1
Cash flows		**(18)**	**65**	**136**	**217**	**288**	**293**
Discount period		0.50	1.50	2.50	3.50	4.50	4.50
Discounted cash flows		**(17)**	**56**	**107**	**154**	**186**	**2,428**

* Including other finance income (expenses), net

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❿ Cellular segment - Valuation results

Valuation Summary

Valuation Results	NIS million
Value of operations from the model years	486
Value of operations from the benchmark year	2,428
Total value of operations	**2,914**

In conclusion, the value of operations in the cellular segment, based on the above assumptions, as at December 31, 2018, is NIS 2,914 million. According to information given to us by Bezeq, the carrying amount of this segment in its books was NIS 2,149 million, therefore, there is no need for impairment.

Development of the value of Pelephone (compared to our previous valuations)

Description	NIS millions
Pelephone valuation as at December 31, 2017	5,403
% change	(15.9%)
Pelephone valuation as at June 30, 2018	3,907
% change	(27.7%)
Pelephone valuation as at December 31, 2018	2,914
% change	(25.4%)

Sensitivity Analysis

The valuation conducted by Prometheus is based on partial implementation of a stand-alone restructuring plan. However, the Company's management expects that it will be possible to implement the restructuring plan in full and even more, utilizing the synergies between Pelephone, YES and Bezeq International.

A review of the effect of the restructuring plan on the value of operations shows that even in a scenario in which the Company does not perform any restructuring measures, the value of operations as at December 31, 2018 is higher than the carrying amount in Bezeq's books.

❿ Cellular segment - Valuation results

Sensitivity Analysis

Sensitivity analysis of the value of operations in the cellular segment for changes in the discount rate and permanent growth:

		Discount rate				
		8.3%	**9.3%**	**10.3%**	**11.3%**	**12.3%**
Permanent growth	**1.5%**	3,511	3,004	2,613	2,304	2,054
	2.0%	3,768	3,191	2,754	2,414	2,141
	2.5%	4,069	3,405	2,914	2,536	2,237
	3.0%	4,427	3,654	3,095	2,673	2,343
	3.5%	4,861	3,945	3,303	2,827	2,461

Conclusion

An increase (decrease) of 1% in the discount rate leads to an increase (decrease) in the value of Pelephone's operation in the range of between NIS 299 million and NIS 664 million. An increase (decrease) of 0.5% in the discount rate leads to an increase (decrease) in the value of Pelephone's operation in the range of between NIS 141 million and NIS 208 million.

Sensitivity Analysis

Sensitivity analysis of the value of operations in the cellular segment for changes in the ARPU of the Company's subscribers:

	Change in ARPU in NIS				
	(2)	**(1)**	**0**	**1**	**2**
Value of operations	2,323	2,619	**2,914**	3,209	3,503

Conclusion

An increase (decrease) of NIS 1 in the ARPU leads to an increase (decrease) in the value of Pelephone's operations of NIS 295 million.

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Appendices

⑩WACC - Cellular segment

Calculation of Discount Rate - Cellular Operations

Marking	Parameter	Value	Remarks
D/V	Debt to asset value ratio	0.21	*Based on the median of the comparison companies (see the table on the left)*
E/V	Equity to balance sheet ratio	0.79	**(D/V) = 1 - (E/V)**
D/E	Debt to equity ratio	0.25	**(E/V) (D/V)/ = (D/V)**
βUL	**Unlevered Beta of benchmark companies**	**0.76**	*To assess the beta of the operations, we chose a group of similar companies. According to our test, there are no traded companies with the identical operations to those assessed. Therefore, we chose companies with some of the same characteristics as those of the operations, but which are different from each other, to create a mix that better expresses its characteristics. The beta is calculated on a weekly basis for a period of five years.*
Tax	Long-term tax rate of operations	23.0%	Long-term tax rate of assessed operations
βL	**Unlevered Beta of operations**	**0.91**	**βL= βUL*{1+(1-Tax)*(D/E)}**
Rf	Risk-free interest	3.2%	*Multi-annual nominal yield to maturity of NIS government bonds for a period of 15 years as at December 31, 2018*
MRP	Market premium	5.9%	*Risk premium in the Israeli market based on Damodaran data updated to 2018*
SRP	Specific Risk Premium	3.5%	*Premium for increase based on Duff and Phelps data for 2018 for medium-sized companies*
Re	**Cost of Equity**	11.99%	**RE = Rf + βL * MRP + SRP**
Rd	**Cost of Debt of the Company**	4.6%	*Price of long-term debt of operations - based on yield to maturity at the valuation date of debentures with an AA rating*
WACC	**Weighted Average Cost of Capital**	**10.27%**	**WACC = Re *(E/V) + Rd*(D/V)*(1-TAX)**

The above table sets out the calculation of a discount rate of operations as at December 31, 2018 of 10.3%.

Additional information about the benchmark companies

Company	Unlevered Beta	D/V
Partner	0.82	0.24
Cellcom	0.63	0.48
Telenor	0.78	0.18
O2	0.73	0.15
US Cellular Corp.	0.80	0.17
Orange Belgium	0.62	0.23
Median	**0.76**	**0.21**

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Appendix B

➓

Carrying amount - Cellular segment

Breakdown of carrying amount of the cellular segment (Pelephone) as at December 31, 2018, as given to us by Bezeq:

Section	Value (NIS millions)
Operating assets, net	* 2,421
Operating liabilities	(1,299)
Excess cost-goodwill for Pelephone recorded in Bezeq's books	1,027
Total carrying amount of Pelephone in Bezeq's books	**2,149**

* Pelephone's net operating assets do not include trade receivables for the sale of terminal equipment in installments (financial instrument).

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