"BEZEQ" THE ISRAEL TELECOMMUNICATION CORP. LIMITED

CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2006

(UNAUDITED)

Condensed Interim Consolidated Financial Statements as at March 31, 2006 (unaudited)

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The Board of Directors of
"Bezeq" - The Israel Telecommunications Corp. Limited

Dear Sirs,

Re: Review of the Unaudited Condensed Interim Consolidated Financial Statements as at March 31, 2006

At your request, we have reviewed the condensed interim consolidated balance sheet of "Bezeq" - The Israel Telecommunications Corp. Limited (hereinafter "Company") as at March 31, 2006, as well as the condensed interim consolidated statements of operations, the condensed interim statements of changes in shareholders' equity and the condensed interim consolidated statements of cash flows for the three-month period then ended.

Our review was carried out in accordance with procedures prescribed by the Institute of Certified Public Accountants in Israel. The procedures included, inter alia, reading the said financial statements, reading the minutes of meetings of the shareholders and of the Board of Directors and its committees, as well as making inquiries of persons responsible for financial and accounting matters.

Reports of other auditors were furnished to us which relate to the review of the condensed interim financial statements of consolidated subsidiaries, whose assets as at March 31, 2006, constitute approximately 37% of the total assets included in the condensed interim consolidated balance sheet and whose revenues constitute approximately 61% of the total revenues included in the condensed interim consolidated statement of operations for the three-month period then ended. Furthermore, reports of other auditors were furnished to us which relate to investments in affiliated companies in which the Company's investments amount to approximately NIS 87 million as at March 31, 2006, and the Company's share in the losses in respect thereof amount to approximately NIS 1 million for the three-month period then ended.

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

In the course of our review, including reviewing the reports of other auditors as mentioned above, nothing came to our attention which would indicate the necessity of making material changes to the said interim financial statements in order for them to be in conformity with generally accepted accounting principles and in accordance with the provisions of Section 4 of the Securities Regulations (Periodic and Immediate Reports), 5730-1970.

We draw attention to the uncertainties relating to the following matters, for which the maximum possible exposure is significant:

1. The continuing opening of the communications sector to competition, changes in tariffs and their effect on the Company's financial position and operating results, as described in Note 1.

2. A program for early retirement as described in Note 5.

3. Contingent claims made against the Company and against invested companies, as described in Note 6A.

4. The financial position of a subsidiary as described in Note 4, including the opinion of the Management of the consolidated company, based on the 2006 work plan and on the alternative business plan, that the prospects of arranging sources of finance required by the consolidated company in the forthcoming year are good.

Somekh Chaikin
Certified Public Accountants (Isr.)

May 23, 2006

Condensed Interim Consolidated Balance Sheets as at

Reported amounts

	March 31 2006 (Unaudited)	March 31 2005 (Unaudited)	December 31 2005 (Audited)
	NIS thousands	NIS thousands	NIS thousands
Current assets			
Cash and cash equivalents	**2,290,703**	1,549,873	2,158,773
Short-term investments	**2,439,802**	1,577,274	2,398,525
Trade receivables	**2,084,237**	2,099,986	2,113,512
Other receivables and debit balances	**385,855**	487,696	321,507
Inventory	**207,525**	304,441	220,404
	7,408,122	6,019,270	7,212,721
Materials and spare parts	**87,639**	137,309	88,881
Broadcasting rights, net	**173,597**	150,617	154,500
Investments and long-term receivables			
Investments, deposits and debit balances	**769,359**	887,189	766,840
Investments in investee companies	**86,509**	69,933	75,467
	855,868	957,122	842,307
Fixed assets			
Cost	**30,839,518**	34,632,903	30,627,629
Less– accumulated depreciation	**21,229,767**	24,128,266	20,684,981
	9,609,751	10,504,637	9,942,648
Other assets			
Goodwill	**1,699,546**	1,769,379	1,699,546
Deferred charges and other assets	**365,653**	387,007	380,483
Deferred taxes	**324,176**	438,686	344,786
	2,389,375	2,595,072	2,424,815
	20,524,352	20,364,027	20,665,872

	March 31 2006 (Unaudited)	March 31 2005 (Unaudited)	December 31 2005 (Audited)
	NIS thousands	NIS thousands	NIS thousands
Current liabilities			
Bank credit	**121,497**	103,561	75,191
Current maturities of:			
Long-term bank loans	**1,221,193**	918,637	1,262,583
Debentures	**436,807**	302,914	527,167
Trade payables	**1,157,644**	1,375,675	1,400,714
Employee severance benefits	**565,706**	634,337	567,878
Other current liabilities	**1,458,283**	1,429,857	1,387,955
Dividend proposed	**1,200,000**	-	-
	6,161,130	4,764,981	5,221,488
Long-term liabilities			
Long-term loans	**2,046,286**	2,813,357	2,151,960
Debentures	**4,902,063**	4,398,407	4,903,056
Employee severance benefits	**277,937**	612,947	297,427
Other long-term liabilities	**53,564**	30,038	34,081
Loans extended by the minority in a subsidiary:			
Loans	**1,118,506**	1,064,057	1,114,498
Less – minority share in deficit of a subsidiary	**(1,118,506)**	(1,064,057)	(1,114,498)
	7,279,850	7,854,749	7,386,524
Minority rights	**-**	(1,177)	-
Contingent liabilities (Note 6)			
Shareholders' equity	**7,083,372**	7,745,474	8,057,860
	20,524,352	20,364,027	20,665,872

Menachem Inbar	**Yacov Gelbard**	**Ron Eilon**
Member of the Board (Chairman of the approval meeting)	President & CEO	Deputy CEO and CFO

Date of approval of the financial statements: May 23, 2006.

The notes to the interim financial statements are an integral part thereof.

Condensed Interim Consolidated Statements of Operations

Reported amounts

	For the three-month period ended March 31		For the year ended December 31
	2006 (Unaudited)	2005 (Unaudited)	2005 (Audited)
	NIS thousands	NIS thousands	NIS thousands
Revenues (Note 8)	**2,819,255**	2,773,123	11,098,686
Costs and expenses			
Operating and general expenses (Note 9)	**1,783,650**	1,763,851	7,193,468
Depreciation	**571,830**	577,507	2,330,711
Royalties to the Government of Israel	**63,194**	65,552	257,429
	2,418,674	2,406,910	9,781,608
Operating income	**400,581**	366,213	1,317,078
Financing expenses, net	**(71,973)**	(54,876)	(417,309)
Earnings after financing expenses	**328,608**	311,337	899,769
Other income, net (Note 10)	**9,382**	87,614	109,386
Earnings before income tax	**337,990**	398,951	1,009,155
Income tax	**(113,502)**	(132,870)	(429,594)
Earnings after income tax	**224,488**	266,081	579,561
Equity in earnings (losses) of affiliates	**1,050**	(3,321)	(12,645)
Minority share in losses (earnings) of subsidiaries	**(26)**	1,947	8,942
Earnings before the cumulative effect of a change in an accounting method	**225,512**	264,707	575,858
Cumulative effect of a changes in accounting method as at the beginning of the year	**-**	15,000	15,000
Net earnings	**225,512**	279,707	590,858
Primary and diluted earnings per share (in NIS)			
Earnings before the cumulative effect of a change in accounting method	**0.087**	0.102	0.222
Cumulative effect of a change in accounting method as at the beginning of the year	**-**	0.005	0.005
Net earnings per share	**0.087**	0.107	0.227

The notes to the interim financial statements are an integral part thereof.

Condensed Interim Statements of Changes in Shareholders' Equity

Reported amounts

	Share capital	Capital reserve – share premium	Capital reserve in respect of transactions between the Company and a controlling shareholder	Dividend proposed after the balance sheet date	Retained earnings (deficit)	Total
Three months ended March 31, 2006						
Balance as at December 31, 2005 (audited)	**6,309,133**	**1,623,423**	**39,010**	**1,200,000**	**(1,113,706)**	**8,057,860**
Net earnings (unaudited)	**–**	**–**	**–**	**–**	**225,512**	**225,512**
Dividend (unaudited)	**–**	**–**	**–**	**(1,200,000)**	**–**	**(1,200,000)**
Balance as at March 31, 2006 (unaudited)	**6,309,133**	**1,623,423**	**39,010**	**–**	**(888,194)**	**7,083,372**
Three months ended March 31, 2005						
Balance as at December 31, 2004 (audited)	6,309,133	1,623,423	37,775	–	(504,564)	7,465,767
Net earnings (unaudited)	–	–	–	–	279,707	279,707
Balance as at March 31, 2005 (unaudited)	6,309,133	1,623,423	37,775	–	(224,857)	7,745,474
Year ended December 31, 2005						
Balance as at December 31, 2004 (audited)	6,309,133	1,623,423	37,775	–	(504,564)	7,465,767
Net earnings (audited)	–	–	–	–	590,858	590,858
Payment by the State in respect of Company privatization (audited)	–	–	1,235	–	–	1,235
Dividend proposed for payment (audited)	–	–	–	1,200,000	(1,200,000)	–
Balance as at December 31, 2005 (audited)	6,309,133	1,623,423	39,010	1,200,000	(1,113,706)	8,057,860

The notes to the interim financial statements are an integral part thereof.

Condensed Interim Consolidated Statements of Cash Flows

Reported amounts

	For the three-month period ended March 31		For the year ended December 31
	2006	2005	2005
	(Unaudited)	(Unaudited)	(Audited)
	NIS thousands	NIS thousands	NIS thousands
Cash flows from operating activities			
Net earnings	**225,512**	279,707	590,858
Adjustments to reconcile net earnings to cash flows from operating activities (see A below)	**522,420**	312,057	2,127,730
Net cash generated by operating activities	**747,932**	591,764	2,718,588
Cash flows used for investing activities			
Investment in fixed assets	**(306,135)**	(475,508)	(1,694,071)
Proceeds from disposal of fixed assets and sale of operation	**13,655**	12,568	147,810
Investment in long-term deposits and investments	**(3,491)**	-	(10,068)
Proceeds from long-term deposits and investments	**3,593**	6,318	91,431
Increase in short-term investments, net	**(30,753)**	(275,089)	(972,260)
Investment in investee companies	**(9,491)**	(2,628)	(18,836)
Investment in other assets	**(16,541)**	(23,760)	(91,893)
Net cash used for investing activities	**(349,163)**	(758,099)	(2,547,887)
Cash flows from financing activities			
Issue of other debentures (after deduction of issue expenses)	**-**	812,295	1,702,265
Repayment of other debentures	**(148,968)**	(91,603)	(267,332)
Receipt of long-term loans	**-**	114,500	474,521
Repayment of long-term loans	**(164,177)**	(591,550)	(1,365,578)
Receipt (repayment) of short-term bank credit, net	**46,306**	15,459	(12,911)
Net cash generated by (used for) financing activities	**(266,839)**	259,101	530,965
Increase in cash and cash equivalents	**131,930**	92,766	701,666
Balance of cash and cash equivalents at the beginning of the period	**2,158,773**	1,457,107	1,457,107
Balance of cash and cash equivalents at the end of the period	**2,290,703**	1,549,873	2,158,773

The notes to the interim financial statements are an integral part thereof.

Condensed Interim Consolidated Statements of Cash Flows (Contd.)

Reported amounts

	For the three-month period ended March 31		For the year ended December 31
	2006	2005	2005
	(Unaudited)	(Unaudited)	(Audited)
	NIS thousands	NIS thousands	NIS thousands
A – Adjustments to reconcile net earnings to net cash flows generated by operating activities			
Revenue and expenses not involving cash flows:			
Depreciation	**571,830**	577,507	2,330,711
Deferred taxes	**31,654**	40,859	144,035
Company's equity in losses (profits) of affiliated companies	**(1,050)**	3,321	12,645
Minority share in earnings (losses) of a subsidiary	**26**	(1,947)	(8,942)
Decrease in employee severance benefits, net	**(21,662)**	(25,286)	(407,265)
Loss from disposal of fixed assets	**(9,576)**	(1,730)	(5,715)
Provision for decrease in value of investments	**-**	-	5,868
Gain from sale of operation	**-**	(101,860)	(103,869)
Exchange rate differences, linkage and interest on long-term deposits and investments	**(1,729)**	21,839	22,170
Exchange rate differences and linkage on short-term investments, net	**(10,524)**	(14,376)	(60,396)
Exchange rate differences and linkage of long-term liabilities:			
Debentures	**66,166**	(84,391)	(69,730)
Long-term loans and other liabilities	**15,428**	25,489	129,032
Amortization of other assets and deferred expenses	**21,693**	47,936	196,015
Changes in asset and liability items:			
Increase in broadcasting rights	**(19,097)**	(10,121)	(14,004)
Decrease (increase) in trade receivables	**28,383**	(8,270)	(63,298)
Decrease (increase) in other receivables and debit balances	**(47,146)**	(29,244)	24,600
Decrease in inventory	**11,037**	5,740	75,943
Decrease (increase) in materials and spare parts	**(18,172)**	(35,935)	24,952
Decrease in trade payables	**(165,968)**	(142,772)	(112,461)
Increase in other current liabilities	**70,328**	62,635	20,733
Increase (decrease) in deferred revenues	**799**	(17,337)	(13,294)
	522,420	312,057	2,127,730
B – Non-cash transactions			
Acquisition of fixed assets, other assets, materials and spare parts on credit	**53,612**	122,859	124,719
Sale of fixed assets on credit	**28,977**	131,408	17,089

The notes to the interim financial statements are an integral part thereof.

Notes to the Financial Statements as at March 31, 2006

NOTE 1 – GENERAL

A. These interim statements were prepared according to generally accepted accounting principles, applicable to the preparation of financial statements for interim periods pursuant to Accounting Standard 14 of the Israeli Accounting Standards Board (hereinafter – the IASB) and to the provisions of Section 4 of the Securities Regulations (Periodic and immediate reports), 5730-1970.

B. These statements should be read in conjunction with the annual financial statements of the Company and its subsidiaries as at December 31, 2005 and for the year then ended, and their accompanying notes (hereinafter – the Annual Reports).

C. The Company presents in the notes to the interim financial statements only those significant changes in its business and legal environment that occurred from the date of the latest annual financial statements until the date of these interim financial statements. The full and detailed description, including significant changes and developments which occurred in recent years, particularly in the fields of cellular telephone services, international communication services, domestic communication services, multi-channel television services, and the opening of those markets to competition, appear in Note 1 to the Company's annual financial statements as at December 31, 2005. The significant changes that occurred from the date of the annual financial statements to the date of these financial statements are as follows:

(1) Further to Note 1(C) to the financial statements as at December 31, 2005, concerning the gradual reduction in the rate of royalties from 3.5% to 3%. The Ministry of Communications notified the Company that the amendment to the Royalty Regulations will be implemented shortly.

(2) Further to Note 1(D) to the financial statements as at December 31, 2005, concerning an appeal filed by the Company in 2001 in the Antitrust Court to change the announcement of the Company's monopoly in the basic telephony service (fixed-line domestic telephony) – following the Company's request that the court expedite the hearing of the appeal, the Company agreed, at the proposal of the court, to withdraw the appeal, and it intends to file a new and revised application to the Antitrust Commissioner. In the opinion of the Company, the fixed-line telephony market is an alternative market for cellular telephony, and this fact is reinforced by new and up-to-date data which have accumulated during the period since the start of the proceeding before the court.

(3) Further to Note 1(E)(1)(a) to the financial statements as at December 31, 2005, concerning an update to the Company's tariffs, the next tariff update is expected to be on June 1, 2006, although as of the date of the publication of these statements the Company has not yet received the relevant draft Regulations.

(4) Further to Note 1E(1)(c) to the financial statements as at December 31, 2005, concerning regulations relating to proceedings and conditions for receipt of a special general license for providing fixed-line domestic communications services without a universal obligation – to the best of the Company's knowledge, during the first quarter of 2006 another two licenses were granted to two additional operators. The subsidiary Bezeq International Ltd. has filed an application for such a license.

(5) Further to Note 1(E)(1)(f) to the financial statements as at December 31, 2005, concerning the numbering and number portability plan, during February/March 2006 there was a further exchange of letters on the matter of the operators', including the Company, inability to meet the timetables that were set. The Company once again notified that it is preparing for the implementation of number portability but for real and technical reasons, it cannot meet the timetable set for implementation of the plan, and it reserves its legal rights in the matter.

(6) Further to Note 1(H) to the financial statements as at December 31, 2005, concerning resolutions adopted by the Board of Directors of the Company on March 1, 2006 to recommend to the General Meeting of the shareholders of the Company the distribution of a cash dividend to the shareholders in the amount of NIS 1,200,000,193, which as at the date of the distribution constitutes NIS 0.4606446 per share and 46.06446% of the Company's issued and paid up capital – the Special General Meeting

NOTE 1 – GENERAL (CONTD.)

C. (CONTD.)

(6) (contd.)

of the shareholders of the Company which convened on March 23, 2006, approved the distribution of the dividend. The dividend was distributed on April 16, 2006.

(7) The Ministry of Communications notified the Company on May 9, 2006 of its intention to call in a guarantee of NIS 7 million out of the bank guarantee of $10 million which the Company deposited for securing fulfillment of the terms of its license, due to its position that the Company launched a campaign in a way which deviates from the rules of the regulation applicable to campaigns. The position of the Company is that it does not require the approval of the Ministry for marketing campaigns. The Company intends to find every legal method available to it in this matter and at the initial stage, the Company is filing an appeal to the Minister of Communications regarding the decision.

(8) On May 11, 2006 the Company received a communication from the Antitrust Authority in the matter of complaints by certain communications operators about actions that were allegedly taken by the Company vis-à-vis these operators. According to the said operators, the said actions constitute abuse of the Company's monopolistic power. The Company has been asked to send data and replies to the questions that were "detailed" in the letter and is sending the requested information.

(9) On May 23, 2006 investigators from the Antitrust Authority appeared at the offices of the Company and presented an order from the Magistrates' Court permitting them to conduct a search at the offices of the Company and to seize any document or object required for an investigation. According to the order, the grounds for issuing the order was the alleged abuse of the status of the monopoly under Section 29A of the Antitrust Law, along with Section 47A (4A) of the Antitrust Law and/or an unreasonable refusal to supply an asset or service under the monopoly, as per Section 29 of the Antitrust Law. During the search, which has not yet been completed, various documents were collected by the investigators, including computerized material, and a number of employees were asked to accompany the investigators to the offices of the Antitrust Authority for interrogation. The Company is cooperating fully with the Authority's investigators.

NOTE 2 – REPORTING PRINCIPLES AND ACCOUNTING POLICY

A. GENERAL

The significant accounting policies applied in thee financial statements are consistent with those applied in the Annual reports, except as stated in this Note.

B. INITIAL APPLICATION OF ACCOUNTING STANDARDS

(1) Accounting Standard No. 20 (Amended) – Accounting treatment of goodwill and intangible assets in the acquisition of an investee company

Commencing January 1, 2006, the Company has applied Accounting Standard No. 20 (Amended) ("the Standard") of the IASB. The Standard prescribes the accounting treatment for goodwill and intangible assets upon acquisition of a subsidiary and of an investee company which is not a subsidiary, including a company under joint control.

The principle changes set out in the Standard compared with the principles applied in the past, are attribution of the surplus cost of the acquisition of investment in an investee company also to identifiable intangible assets of the acquired company; a distinction between intangible assets with a defined useful life and intangible assets of an indefinite useful life; immediate recognition as gain, on the date of acquisition, in the statement of income, of negative goodwill created in

NOTE 2 – REPORTING PRINCIPLES AND ACCOUNTING POLICY (CONTD.)

B. INITIAL APPLICATION OF ACCOUNTING STANDARDS (CONTD.)

(1) (contd.)

the acquisition after deduction of intangible assets and non-financial assets of the investee company; termination of the systematic deduction of positive goodwill and intangible assets with an indefinite useful life; distinction between goodwill of a subsidiary and of an investee company which is not a subsidiary for the matter of impairment. Comparative figures were not restated.

The amount of goodwill amortized in the corresponding period and in the year 2005 amounted to NIS 23,279 thousand and NIS 93,112 thousand, respectively. (see also note 10).

(2) Accounting Standard No. 21 – Earnings per share

Commencing January 1, 2006, the Company has applied Accounting Standard No. 21 (Amended) ("the Standard") of the IASB. Pursuant to the Standard, the Company computes the basic earnings per share with regard to profit or loss, as well as the basic earnings per share with regard to profit or loss from ongoing operations, attributed to the ordinary shareholders. The basic earnings per share is calculated by dividing the profit or loss attributed to the ordinary shareholders, by the weighted average of the number of ordinary shares in circulation during the period. For the purpose of calculating diluted earnings per share, the Company adjusted the profit or the loss attributed to the ordinary shareholders, and the weighted average of the number of ordinary shares in circulation, in respect of the effects of all the diluting potential ordinary shares. The Company's equity in the earnings of investee companies was computed according to its equity in the earnings per share of those companies, multiplied by the number of shares the Company holds. The initial application of the Standard did not affect the earnings per share of the Company.

(3) Accounting Standard No. 22 – Financial instruments: disclosure and statement

Commencing January 1, 2006, the Company has applied Accounting Standard No. 22 ("the Standard") of the IASB. The Standard sets out the rules for the stating financial instruments in the financial statements and details the proper disclosure required for them. In addition, the Standard determines the manner of classification of financial instruments as financial liability and as shareholders' equity, the classification of interest, dividends, related losses and gains, and the circumstances in which financial assets and financial liabilities should be set off. The Standard cancels Opinion 53 – Accounting treatment of convertible liabilities, and Opinion 48 – Accounting treatment of option warrants. The Standard was adopted "from now on". Comparison figures relating to prior periods were not restated. Following the initial adoption of the accounting standard, the Company offset deferred issuance expenses in the amount of NIS 9 million from the debentures and loan items.

(4) Accounting Standard No. 24 – Share-based payment

Commencing January 1, 2006, the Company has applied Accounting Standard No. 24 ("the Standard") of the IASB. Pursuant to the provisions of the Standard, the Company will recognise share-based payment transactions in its financial statements including transactions with employees or other parties that must be settled in equity instruments, in cash or by other assets. Share-based payment transactions in which goods or services are received will be reported at their fair value.

Regarding transactions which are cleared in capital instruments, the Standard applies to grants made after March 15, 2005 but which had not yet vested by January 1, 2006. In the same manner, the Standard applies to changes which occurred in the terms of the transactions cleared in capital instruments which were made after March 15, 2005, even if the grants in

NOTE 2 – REPORTING PRINCIPLES AND ACCOUNTING POLICY (CONTD.)

B. INITIAL APPLICATION OF ACCOUNTING STANDARDS (CONTD.)

(4) (contd.)

respect of which the changes were made were prior to that date. The initial application of the Standard did not affect the results of operations and the financial condition of the Company.

(5) Accounting Standard No. 25 – Income

Commencing January 1, 2006, the Company has applied Accounting Standard No. 25 ("the Standard") of the IASB. The Standard deals with recognition of income from three types of transactions: the sale of goods, the provision of services, and the made by others of the company's interest-yielding assets, royalties and dividends, and it prescribes the accounting treatment required (rules of recognition, measurement and disclosure) for those three types of transaction. The initial application of the Standard did not materially affect the results of operations and the financial condition of the Company.

As of January 1, 2006 the Company has applied the IASB published Clarification No. 8 – "Reporting income on a gross basis or a net basis" ("the Clarification"). The Clarification is based on the professional publication EITF 99-19 of the Emerging Issues Task Force in the U.S.A. According to the Clarification, an entity operating as an agency or as a broker without bearing the risks and yields deriving from the transaction, will state its income on a net basis. Conversely, an entity operating as a principal supplier and bearing the risks and yields deriving from the transaction will state its income on a gross basis. The Clarification provides a list of indicators to be considered in order to determine the basis on which income should be reported – gross or net. Since in the past the Company treated the matter of gross or net income in accordance with the provisions of EITF 99-19, the initial application of the new Clarification did not influence the Company in any way.

NOTE 3 – RATES OF CHANGES IN THE CONSUMER PRICE INDEX AND FOREIGN CURRENCY EXCHANGE RATES

The changes that occurred in the consumer price index and in the exchange rates of the US dollar and the euro in the period of account, are as follows:

	Consumer price index	Exchange rate of the US dollar	Exchange rate of the euro
	%	%	%
For the three-month period ended:			
March 31, 2006	**0.583**	**1.347**	**3.964**
March 31, 2005	(0.596)	1.230	3.879
For the year ended December 31, 2005	2.386	6.848	(7.334)

Notes to the Financial Statements as at March 31, 2006

NOTE 4 – INVESTMENTS IN INVESTEE COMPANIES

A. D.B.S. SATELLITE SERVICES (1998) LTD. ("DBS")

In January 1999, DBS received a license from the Ministry of Communications for satellite television broadcasts, and commenced the provision of services in July 2000. Since starting operations, DBS has accumulated considerable losses. The loss for 2005 amounted to approximately NIS 328 million and the loss for the three-month period ended March 31, 2006, amounted to approximately NIS 67 million. As a result of these losses, DBS's capital deficit and working capital deficit as at March 31, 2006 amount to approximately NIS 3,638 million and NIS 510 million respectively.

The Company's investment in DBS (mainly shareholders' loans) as at the balance sheet date is approximately NIS 1,562 million (before interest and linkage). The Company's equity in the accumulated losses of DBS since its investment (excluding deduction of goodwill) is approximately 1,639 million, of which approximately NIS 64 million was recorded in the reporting period (DBS's losses for the period, net of the increase in new loans given by minority shareholders). The balance of DBS's current debt to the Company and its consolidated companies amounts to approximately NIS 83 million.

The terms of the long-term loans which DBS received from banks, the balance of which as at March 31, 2006 is NIS 1,324 million (including current maturities), impose various restrictions on DBS, which include, *inter alia* – restrictions relating to encumbrance or sale of certain assets, restrictions on receipt of credit from other banks without prior approval, a restriction on repayment of shareholders loans, and a demand to comply with financial criteria ("the Conditions"). As at March 31, 2006, DBS is in compliance with the Conditions prescribed in the financing agreements (after a benefit which was granted in connection with the financial criteria in respect of the first quarter of 2006). In view of the projections of the Management of DBS regarding its business results for 2006, DBS is working with the banks to revise the financial directives in the financing agreement. DBS is also negotiating with the banks to settle a dispute relating to insurance obligations prescribed in the financing agreement.

In March 2006 Israel Aircraft Industries Ltd. ("IAI") contacted DBS and demanded full repayment of DBS's debt to IAI in the wake of DBS's failure to adhere to the payment arrangement that was determined between the parties. As at the date of approval of the financial statements, DBS is conducting talks with IAI in order to arrive at a solution that will be acceptable to both parties. A delay in payment to IAI constitutes a *prima facie* breach of the financing agreement, but the banks have confirmed to DBS that they will not deem IAI's demand for the repayment of the loan and the non-payment on the part of DBS a breach of the financing agreement, provided IAI does not take any steps whatsoever in order to collect the said debt by August 1, 2006 and that a written repayment solution is agreed between the parties by that date.

In March 2004, the Board of Directors of the Company approved an investment of NIS 440 million in DBS by the end of 2005 ("the Additional Injection"), of which, by October 11, 2005, the Company had transferred approximately NIS 284 million.

On December 31, 2004, and February 14, 2005, the Company and DBS were notified of decisions of the then Minister of Communications relating to the Additional Injection. Those decisions determined, *inter alia*, that –

(1) The total amount of the planned Additional Injection (NIS 440 million) was limited to a maximum of NIS 350 million.

(2) With regard to the NIS 195 million of the Additional Injection already transferred by the Company at that time to DBS, no additional action was taken.

(3) The balance of the sum, a maximum of NIS 155 million, would be transferred once every quarter in equal portions during 2005.

(4) The Company would not be permitted to provide a guarantee to the shareholders of DBS, to banks or to institutional financing entities, or to make any other similar commitment, for securing their part in the Additional Injection or in credit granted to DBS by them.

Notes to the Financial Statements as at March 31, 2006

NOTE 4 – INVESTMENTS IN INVESTEE COMPANIES (CONTD.)

A. D.B.S. SATELLITE SERVICES (1998) LTD. ("DBS") (CONTD.)

In April and May 2005, the Company and DBS filed petitions in the High Court of Justice for grant of an order *nisi* against the Minister of Communications, declaring that the decisions described above are null and void. The petitions, which were heard on October 11, 2005, raised questions of principle which are far from simple, both factually and legally, and which were brought into sharp focus during the hearing. The Court has not yet given its decision.

On March 21, 2006, the Company received a letter from the Minister of Communications, stating that after examining the implications of further injections of funds into DBS for the promotion and consolidation of competition in fixed-line domestic communications, and since the business plan of DBS for 2006 calls for injections in 2006 amount to NIS 55 million, the Minister of Communications was considering placing a limit on injections of funds in 2006 in the following manner:

(1) The Company's share in the total injections into DBS would not exceed 40%.

(2) The share of the other DBS shareholders and of the banks or financing institutions would not exceed 60%.

(3) The Company or an entity acting on its behalf would not provide a guarantee to the shareholder, the banks or institutional financing entities, or any similar commitment, for securing their part in the injections or in credit granted by them to DBS.

(4) Towards the end of 2006, the subject of the injections, insofar as may be required in future years, would be re-examined.

The Company sent its response to the letter on April 2, 2006, in which it gave notice that it opposes the decision being considered by the Ministry of Communications, which it believes to be *ultra vires*, and requesting a hearing to explain its position and make its arguments orally before the Minister of Communications.

On January 31, 2006, the Board of Directors of DBS approved its budget for 2006, which requires that DBS obtains additional external financing for the year. As at the date of approval of the financial statements, DBS is working to obtain additional financial resources which will enable it to achieve the goals of the budget for the coming year. If those resources cannot be obtained, DBS will operate in accordance with an alternative business plan which does not necessitate additional resources beyond the existing ones. The Management of DBS believes, based on the 2006 budget and on the alternative business plan, that the prospects for arranging the financial resources required by DBS in the coming year are good.

B. GOLDNET COMMUNICATION SERVICES - A REGISTERED PARTNERSHIP ("GOLDNET")

On April 30, 2006 an agreement was signed between the Company, Malam Systems Ltd. and Goldnet Communication Services – a Registered Partnership **("GOLDNET")** of the first part, and the subsidiary Bezeq International of the other part, for the acquisition of all the operations of Goldnet by Bezeq International, in consideration of NIS 6.8 million, which will be divided between the Company (NIS 5.1 million) and Malam Systems (NIS 1.7 million).

Upon fulfillment of all the suspending conditions stipulated in the acquisition agreement (*inter alia* approval by the Antitrust Commissioner and the Ministry of Communications) and payment of the consideration, Goldnet will cease to provide services.

NOTE 5 – LIABILITIES DUE TO TERMINATION OF EMPLOYER-EMPLOYEE RELATIONS

EARLY RETIREMENT PLAN

Pursuant to the foregoing in Note 16D in the financial statements as at December 31, 2005, regarding negotiations that have commenced between Company Management and the employees' representatives in connection with a change in the organizational structure involving employee retirement and/or dismissal and a new collective labor agreement, the negotiations are continuing but have not yet matured to the point of an agreement.

On April 27, 2006, a "notification of a strike or lockout" was received at the offices of the Company in accordance with the Law for the Settlement of Labor Disputes, 5717-1957 ("the Notification"). The Notification pertains to a strike at the Company beginning on May 14, 2006, and thereafter, which was declared by the New General Federation of Labor and was approved, according to the aforementioned, by the representative professional union.

The matters in dispute, according to the aforementioned in the Notification, are:

"A. Severe implications expected to affect the employees as a result of the severe damage to the Company's financial robustness due to the failure to arrange the matter of granting discounts, reducing the Company's royalties, tariff flexibility and in light of the issuing of licenses to competitors on terms that seriously harm the Company.

B. Disregard for the employees' representative and it's requests and conduct that is not in good faith and is unacceptable in collective labor relations in general and in labor relations in the public service in particular."

Following serious disruptions and disconnections that were caused as a result of the employee sanctions, the Company applied to the labor court on May 18, 2006. During the discussion that took place in the labor court, it was decided that the employees would return to work and intensive negotiations would be conducted in order to reach an agreed upon solution through negotiations and not through sanctions and strikes.

NOTE 6 – CONTINGENT LIABILITIES

A. CLAIMS AND CONTINGENT LIABILITIES

The Company and the investee companies have contingent liabilities in respect of which the maximum possible exposure is considerable. A detailed description of these contingent liabilities appears in Note 19A to the annual financial statements of the Company as at December 31, 2005. No material changes in contingent liabilities have occurred up to the date of signing these financial statements, other than the following:

(1) Further to Note 19A(4)b. to the financial statements as at December 31, 2005, concerning a number of claims relating to recognition of various of salary components as pension components and of the notice of a party to the a collective dispute ("the Claim") which was filed by the New General Federation of Workers ("the Histadrut") in the name of all the employees of the Company, in which the Histadrut alleged that grossing up payments, the administrative on-call component and clothing allowances ("the Components") which were and are paid to Company employees, are regular pay, which form part of the determining salary of every employee, including for the calculation of payments upon retirement, redemption of holidays, grants, acclimatization payments, percentage increments and hourly pay value and that various payments and provisions should be made in respect thereof, including for pension purposes.
On April 4, 2006, the decision of the Jerusalem Regional Labor Court dismissed the Claim and all its component parts filed by the Histadrut in the name of all Company employees.

Notes to the Financial Statements as at March 31, 2006

NOTE 6 – CONTINGENT LIABILITIES (CONTD.)

A. CLAIMS AND CONTINGENT LIABILITIES (CONTD.)

(1) (Contd.)

In its decision, the Court allowed in full the argument of the Company, that the conduct of the parties over so many years indicates unequivocally that the demands of the Histadrut directly contradict the agreements applicable in the relations of the parties, which are binding in the circumstances, and therefore those demands should be dismissed. The Court further determined that even if the Components are examined on their merits, the Claim would be dismissed since according to case law, all three Components fall within the definition of ”extras" and not "pay", and therefore do not grant entitlement entitled to the reliefs claimed by the Histadrut.

The financial statements include a provision of NIS 50 million in respect of the administrative on-call component and in respect of another components claim. The Company has examined the significance and implications of the decision and concluded that the conditions have not yet been reached in order to allow for canceling or reducing the provision.

(2) Further to Note 19A(11) to the financial statements as at December 31, 2005, concerning a claim and application for recognition as a class action, in the matter of reimbursement of a commission which the plaintiff alleges was collected unlawfully, for calls in Israel from a public telephone operated by means of a BezeqCard, on April 16, 2006, the applicant filed an application to amend the application for recognition as a class action pursuant to the new Class Actions Law, 5766-2006. The Company opposed the application. The Court has not yet given its decision. In the opinion of the legal advisers who are handling the claim on behalf of the Company, in any case, and even if the plaintiff's application is allowed, following amendment of the Telecommunications Regulations, the basis for the claim and the application for recognition as a class action no longer exists.

(3) Further to Note 19A(14) to the financial statements as at December 31, 2005, concerning the dismissal of a class action filed against the Company in May 2003, alleging that the Company abuses its monopolistic power and collects enormous sums of money from internet users in that it refuses to install splitters on high-speed (ADSL) lines. On March 27, 2006, the plaintiff filed an appeal in the Supreme Court, in which he petitions for the decision of the District Court dismissing his claim to be cancelled. The Company believes, based on the opinion of its external legal advisers, that the chances that the appeal will be allowed are lower than the possibility of the appeal being dismissed.

(4) Further to Note 19A(20) to the financial statements as at December 31, 2005, concerning the dispute between the Company and the Ministry of Communications relating to the payment of royalties in respect of interconnect revenues from cellular subscribers to Company subscribers in the period between April 1999 and the end of 2000, on April 12, 2006, the Company paid the sum of approximately NIS 17 million requested by the Ministry. The Company is in advanced discussions with the Ministry in an attempt to resolve the other disputes related to royalties.

(5) On April 6, 2006, the Company received a claim together with an application for recognition as a class action, which was filed by a private (and inactive) company which is a shareholder of the Company. According to its allegations, the claim concerns the plaintiff being subscribed to the "Free From 7" track and being charged according to that track tariff, without it having ordered the service. According to the plaintiff, it has cause of claim in the circumstances of the matter, under the Consumer Protection Law, 5741-1981, the Contracts Law (General part), 5733-1973, and the Unjust Enrichment Law, 5739-1979. The amount of the personal claim is assessed by the plaintiff at NIS 239.18.

The plaintiff has applied for the claim to be recognized as a class action in the name of all the subscribers who were charged unlawfully in chargeable tracks and for certain services of the Company which are listed in the claim. The plaintiff estimates that the financial loss of the members of the group included in the class action could reach millions of shekels per year. The Company is studying the claim and in unable, at this stage, to assess its chances.

NOTE 6 – CONTINGENT LIABILITIES (CONTD.)

A. CLAIMS AND CONTINGENT LIABILITIES (CONTD.)

(6) On May 15, 2006, the Company received a claim with an application for recognition as a class action, which was filed pursuant to Section 5 of the Class Actions Law, 5766-2006. The Statement of Claim alleges that the Company collected from the plaintiff arrearage interest on amounts of Value Added Tax which the plaintiff should have paid to the Company and which are not part of the services provided by the Company. The amount of the plaintiff's personal claim is NIS 0.33. The plaintiff does not make any assessment of the amount of the class action.
The Company is studying the claim and is unable, at this stage, to estimate its outcome.

(7) Further to Note 19A(34) to the financial statements as at December 31, 2005, concerning notice of the filing of an application to add Pelephone to an appeal proceeding filed by the owners of rights in land adjoining a cellular communication site operated by Pelephone together with others in Ramat Gan. Pelephone's objection to joining the proceeding as a whole was allowed. Pelephone believes, relying on its legal advisers at this stage of the proceeding, that it is at no risk of exposure.

(8) A number of proceedings were recently submitted to Pelephone, in which local committees were requested to add Pelephone as a party to various appeals filed in appeals committees against dismissal of claims of impairment of value under Section 197 of the Planning and Construction Law, in respect of the erection of communications installations. Pelephone is studying each application and making its decisions accordingly. Pelephone believes, relying on its legal advisers, that it is not at risk of material exposure at this stage of these proceedings.

(9) A number of legal proceedings are in progress against Pelephone (whether in administrative petitions, appeals or civil actions), which were filed against the licensing and/or erection of communications sites. Pelephone, the respondent in these proceedings, opposes the reliefs applied for. Pelephone believes, relying on its legal advisers, that it is not at risk of material exposure in these proceedings.

B. FORWARD TRANSACTIONS

Forward Currency Transactions – Hedging Transactions

Consolidated

	Currency purchased	Currency payable	Final repayment date	Amounts receivable	Amounts payable
				NIS millions	
Forward contracts at predetermined exchange rate					
(excluding premium/discount)	Dollar	NIS	September 2006	271	268
	Euro	NIS	August 2007	1,690	1,704
	CPI-linked NIS	NIS	December 2010	1,102	1,146

Futures Currency Transactions – Contracts not for Hedging Purposes

	Purchased currency	Currency payable	Last repayment date	Scope of commitment
				NIS millions
Forward contracts at predetermined exchange rate				
(excluding premium/discount)	Dollar	Shekel	August 2006	383
	Index	Shekel	December 2006	50

Notes to the Financial Statements as at March 31, 2006

NOTE 7 – TRANSACTIONS WITH INTERESTED PARTIES AND RELATED PARTIES

A. Further to Note 27C to the financial statements as at December 31, 2005, on March 23, 2006, the General Meeting of the shareholders of the Company approved the Company entering into an agreement with a company which will be owned and controlled by the shareholders of Ap.Sab.Ar. and will provide the Company with regular management and consultation services, including by means of serving directors and directors who will serve from time to time in the Company and/or in its subsidiaries, for US $1.2 million per year. The term of the agreement is from October 11, 2005 the date of closing the purchase of 30% of the shares of the Company by Ap.Sab.Ar.) to December 31, 2008, unless one of the parties gives the other three months' notice of its wish to terminate it.

B. **BENEFITS FOR DIRECTORS**

On May 15, 2006, the Audit Committee and the Board of Directors approved the terms of employment of the Chairman of the Board who is expected to be elected as Director and Chairman. Below are the details of the terms of his employment:

1 Employment at an 80% position under a personal employment agreement at a monthly salary of NIS 150,000 and related benefits as customary (senior employees' insurance plan, supplementary study fund, Company car, driver, reimbursement of expenses, telephone, etc.).

2. In addition to his regular monthly salary, a once yearly payment (with no conditions of any kind) in the amount of one million two hundred thousand shekels (linked to the Index).

3. The commitment shall be for an undefined period, where each party has the right to bring the commitment to an end by giving three months' notice.

4. Insofar as the Company has an employee stock options plan, the Chairman shall be included in it in accordance with the criteria of that plan.

The terms of employment are subject to the approval of the general meeting of shareholders which will convene on June 21, 2006.

NOTE 8 – REVENUES FROM TELECOMMUNICATION SERVICES

	For the three-month period ended March 31		For the year ended December 31
	2006 (Unaudited)	**2005 (Unaudited)**	**2005 (Audited)**
	NIS thousands	**NIS thousands**	**NIS thousands**
Revenues from communication services –			
Traffic	**340,542**	368,237	1,436,615
Fixed fees	**649,800**	624,370	2,559,559
Total revenues from fixed-line communications	**990,342**	992,607	3,996,174
Cellular telephone	**926,805**	927,364	3,643,795
International communications and internet services	**232,117**	188,566	775,532
Multi-channel television	**314,963**	284,134	1,171,318
Installation and sale of equipment to subscribers	**294,630**	314,207	1,246,947
	2,758,857	2,706,878	10,833,766
Other revenues	**60,398**	66,245	264,920
	2,819,255	2,773,123	11,098,686

Notes to the Financial Statements as at March 31, 2006

NOTE 9 – OPERATING AND GENERAL EXPENSES

	For the three-month period ended March 31		For the year ended December 31
	2006 (Unaudited)	2005 (Unaudited)	2005 (Audited)
	NIS thousands	NIS thousands	NIS thousands
Salaries and related expenses –			
Operations	**455,351**	433,934	1,794,458
General and administrative	**172,076**	162,443	684,290
Total salaries and incidentals	**627,427**	596,377	2,478,748
General expenses	**291,333**	299,514	1,209,169
Materials and spare parts	**202,324**	256,546	1,016,735
Consumption of content from satellite services	**108,442**	100,198	419,309
Cellular telephone expenses	**256,759**	254,521	991,066
Building maintenance	**84,149**	86,807	366,630
Services and maintenance by sub-contractors	**114,301**	105,761	422,416
International communications expenses	**96,406**	64,027	277,210
Vehicle maintenance expenses	**45,402**	40,086	181,385
Collection fees	**12,328**	12,073	49,196
	1,838,871	1,815,910	7,411,864
Less salaries charged to investment in fixed assets	**55,221**	52,059	218,396
	1,783,650	1,763,851	7,193,468

NOTE 10 – OTHER INCOME, NET

	For the three-month period ended March 31		For the year ended December 31
	2006 (Unaudited)	2005 (Unaudited)	2005 (Audited)
	NIS thousands	NIS thousands	NIS thousands
Provision for employee severance benefits upon early retirement	**–**	(7,000)	83,000
Provision for impairment and other liabilities in respect of investments in other companies	**–**	–	(5,868)
Compensation in respect of a settlement agreement	**–**	14,483	14,483
Amortization of goodwill	**–**	(23,279)	(93,112)
Capital gain from sale of operation	**–**	101,860	103,869
Capital gains, net	**9,576**	1,730	5,715
Others	**(194)**	(180)	2,129
Disposal of assets and impairment of value of fixed assets	**–**	–	(830)
	9,382	87,614	109,386

Notes to the Financial Statements as at March 31, 2006

NOTE 11 – POST BALANCE SHEET DATE EVENTS

On May 14, 2006 the Company received notice from Eurofund 2000, a venture capital fund which invests mainly in communications, software, internet, semiconductor and homeland security start-ups ("the Fund"), of a distribution from which the Company, a partner in the Fund, is expected to receive immediately the sum of US $5.7 million.
The distribution follows the sale of approximately 18% of the Fund's holdings in an optical network equipment company, for approximately US $42 million (the Fund's investment in the company was US $2 million).

As a result of the distribution, the Company will record a capital gain (before tax) of approximately NIS 25 million.

NOTE 12 – CONDENSED INTERIM FINANCIAL STATEMENTS OF THE COMPANY

A. STATEMENTS OF OPERATIONS

	For the three-month period ended March 31		For the year ended December 31
	2006 (Unaudited)	2005 (Unaudited)	2005 (Audited)
	NIS thousands	NIS thousands	NIS thousands
Revenues (Note 12B)	**1,170,709**	1,195,718	4,723,734
Costs and expenses			
Operating and general expenses (Note 12C)	**576,593**	562,004	2,346,451
Depreciation	**323,405**	349,395	1,390,435
Royalties to the Government of Israel	**31,020**	35,386	135,575
	931,018	946,785	3,872,461
Operating income	**239,691**	248,933	851,273
Financing expenses, net	**(18,202)**	(5,927)	(80,897)
Earnings after financing expenses	**221,489**	243,006	770,376
Other revenues, net	**11,097**	110,771	201,012
Earnings before income tax	**232,586**	353,777	971,388
Income tax	**(65,200)**	(103,046)	(332,118)
Earnings after income tax	**167,386**	250,731	639,270
Company's equity in earnings (losses) of investee companies	**58,126**	13,976	(63,412)
Earnings before the cumulative effect of a change in accounting method	**225,512**	264,707	575,858
Cumulative effect of a change in accounting method at the beginning of the year	**–**	15,000	15,000
Net earnings	**225,512**	279,707	590,858

Notes to the Financial Statements as at March 31, 2006

NOTE 12 – CONDENSED INTERIM FINANCIAL STATEMENTS OF THE COMPANY (CONTD.)

B. Revenues from telecommunications services

	For the three-month period ended March 31		For the year ended December 31
	2006 (Unaudited)	2005 (Unaudited)	2005 (Audited)
	NIS thousands	NIS thousands	NIS thousands
Domestic fixed-line communications			
Traffic	**346,444**	380,460	1,460,076
Fixed fees	**606,620**	585,894	2,404,970
Total revenues from fixed-line communications	**953,064**	966,354	3,865,046
Cellular telephone	**92,863**	92,660	370,706
International communications	**29,259**	28,519	109,207
Installation and sale of equipment to subscribers and other	**53,219**	54,175	167,904
	1,128,405	1,141,708	4,512,863
Other revenues	**42,304**	54,010	210,871
	1,170,709	1,195,718	4,723,734

C. Operating and general expenses

	For the three-month period ended March 31		For the year ended December 31
	2006 (Unaudited)	2005 (Unaudited)	2005 (Audited)
	NIS thousands	NIS thousands	NIS thousands
Salaries and related expenses –			
Operations	**289,471**	277,467	1,140,482
General and administrative	**77,321**	68,640	288,804
Total salaries and incidentals	**366,792**	346,107	1,429,286
General expenses	**65,232**	73,760	298,767
Materials and spare parts	**18,225**	20,890	97,294
Building maintenance	**76,186**	78,226	320,700
Services and maintenance by sub-contractors	**48,509**	50,141	195,820
International communications expenses	**7,248**	5,075	30,033
Vehicle maintenance expenses	**33,460**	28,430	128,961
Collection fees	**9,308**	8,797	36,735
	624,960	611,426	2,537,596
Less salaries charged to investments in fixed assets	**48,367**	49,422	191,145
	576,593	562,004	2,346,451

Notes to the Financial Statements as at March 31, 2006

NOTE 13 – BUSINESS SEGMENTS

The Company and the investee companies operate in various segments of the communications sector. Data on activities by segment are stated according to the segments of operation of those companies.

	For the three-month period ended March 31, 2006						
	Domestic fixed line communications	**Cellular telephone**	**International communications and Internet services**	**Multi-channel television**	**Others**	**Adjustments**	**Consolidated**
Revenues							
Revenues from external sources	**1,102,787**	**1,084,941**	**239,952**	**326,998**	**64,577**	**–**	**2,819,255**
Inter-segment revenues	**67,922**	**3,484**	**4,899**	**5,049**	**24,623**	**(105,977)**	**–**
Total revenues	**1,170,709**	**1,088,425**	**244,851**	**332,047**	**89,200**	**(105,977)**	**2,819,255**
Segment results*	**239,691**	**139,226**	**33,148**	**(13,835)**	**2,351**	**–**	**400,581**

	For the three-month period ended March 31, 2005						
	Domestic fixed line communications	**Cellular telephone**	**International communications and Internet services**	**Multi-channel television**	**Others**	**Adjustments**	**Consolidated**
Revenues							
Revenues from external sources	1,132,440	1,106,280	193,812	284,394	56,197	–	2,773,123
Inter-segment revenues	63,151	4,040	5,359	4,268	27,246	(104,064)	–
Total revenues	1,195,591	1,110,320	199,171	288,662	83,443	(104,064)	2,773,123
Segment results*	248,933	121,269	20,517	(24,453)	(53)	–	366,213

	For the year ended December 31, 2005						
	Domestic fixed line communications	**Cellular telephone**	**International communications and Internet services**	**Multi-channel television**	**Others**	**Adjustments**	**Consolidated**
Revenues							
Revenues from external sources	4,457,189	4,413,421	795,176	1,200,865	232,035	–	11,098,686
Inter-segment revenues	266,545	14,854	21,488	20,997	104,511	(428,395)	–
Total revenues	4,723,734	4,428,275	816,664	1,221,862	336,546	(428,395)	11,098,686
Segment results*	851,273	466,165	97,978	(99,535)	1,197	–	1,317,078

* Segment results do not include Other revenues (expenses), net, as stated in Note 10.

Notes to the Financial Statements as at March 31, 2006

NOTE 14 – CONDENSED FINANCIAL STATEMENTS OF PELEPHONE COMMUNICATIONS LTD., DBS SATELLITE SERVICES (1998) LTD, AND BEZEQ INTERNATIONAL LTD.

1. PELEPHONE COMMUNICATIONS LTD.

A. Balance sheet

	For the three-month period ended March 31		For the year ended December 31
	2006	2005	2005
	(Unaudited)	(Unaudited)	(Audited)
	NIS thousands	NIS thousands	NIS thousands
Current assets	**1,846,501**	1,472,269	1,881,982
Long-term trade receivables	**334,505**	299,820	338,281
Investment in investee companies	**3,565**	3,521	3,565
Deferred income tax	**–**	73,901	19,799
Fixed assets, net	**2,926,413**	3,055,918	3,009,219
Other assets	**333,805**	335,939	337,787
	5,444,789	5,241,368	5,590,633
Current liabilities	**1,713,509**	1,320,297	1,558,012
Long-term liabilities	**1,567,542**	1,719,959	1,666,193
Shareholders' equity	**2,163,738**	2,201,112	2,366,428
	5,444,789	5,241,368	5,590,633

Notes to the Financial Statements as at March 31, 2006

NOTE 14 – CONDENSED FINANCIAL STATEMENTS OF PELEPHONE COMMUNICATIONS LTD., DBS SATELLITE SERVICES (1998) LTD, AND BEZEQ INTERNATIONAL LTD. (CONTD.)

1. PELEPHONE COMMUNICATIONS LTD. (CONTD.)

B. Statement of Operations

	For the three-month period ended March 31		For the year ended December 31
	2006 (Unaudited)	2005 (Unaudited)	2005 (Audited)
	NIS thousands	NIS thousands	NIS thousands
Revenues from Pelephone services, sales and services	**1,088,424**	1,110,321	4,428,277
Cost of Pelephone services, sales and services	**826,813**	859,151	3,415,885
Gross profit	**261,611**	251,170	1,012,392
Sales and marketing expenses	**99,230**	104,980	432,808
General and administrative expenses	**23,154**	24,917	107,218
	122,384	129,897	540,026
Operating income	**139,227**	121,273	472,366
Financing expenses, net	**(3,382)**	(10,127)	(115,264)
Other revenues (expenses), net	**(1,407)**	42	1,136
Earnings before income tax	**134,438**	111,188	358,238
Income tax	**(37,128)**	(36,602)	(113,333)
Earnings after income tax	**97,310**	74,586	244,905
Company's equity in losses of an affiliate	**–**	(3,504)	(8,507)
Net earnings	**97,310**	71,082	236,398

Notes to the Financial Statements as at March 31, 2006

NOTE 14 – CONDENSED FINANCIAL STATEMENTS OF PELEPHONE COMMUNICATIONS LTD., DBS SATELLITE SERVICES (1998) LTD, AND BEZEQ INTERNATIONAL LTD. (CONTD.)

2. DBS SATELLITE SERVICES (1998) LTD.

A. Balance sheet

	For the three-month period ended March 31		For the year ended December 31
	2006 (Unaudited)	2005 (Unaudited)	2005 (Audited)
	NIS thousands	NIS thousands	NIS thousands
Current assets	**156,759**	131,581	154,567
Broadcasting rights, net	**173,601**	150,621	154,500
Fixed assets, net	**1,024,583**	1,088,292	1,047,994
	1,354,943	1,370,494	1,357,061
Current liabilities	**666,479**	608,559	613,379
Long-term liabilities	**1,409,791**	1,291,075	1,419,257
Loans from shareholders	**2,916,558**	2,714,884	2,893,024
Capital deficit	**(3,637,885)**	(3,244,024)	(3,568,599)
	1,354,943	1,370,494	1, 357,061

B. Statement of Operations

	For the three-month period ended March 31		For the year ended December 31
	2006 (Unaudited)	2005 (Unaudited)	2005 (Audited)
	NIS thousands	NIS thousands	NIS thousands
Revenues from DBS services	**332,046**	288,662	1,221,863
DBS operating expenses	**288,694**	256,574*	1,099,364*
Gross profit	**43,352**	32,088	122,499
Sales and marketing expenses	**31,611**	33,264*	131,136*
General and administrative expenses	**22,610**	20,144	77,055
	54,221	53,408	208,191
Operating loss	**(10,869)**	(21,320)	(85,692)
Financing expenses, net	**(56,194)**	(39,419)	(241,335)
Other expenses, net	**(201)**	(80)	(830)
Net loss	**(67,264)**	(60,819)	(327,857)

* Reclassified

Notes to the Financial Statements as at March 31, 2006

NOTE 14 – CONDENSED FINANCIAL STATEMENTS OF PELEPHONE COMMUNICATIONS LTD., DBS SATELLITE SERVICES (1998) LTD, AND BEZEQ INTERNATIONAL LTD. (CONTD.)

3. BEZEQ INTERNATIONAL LTD.

A. Balance sheet

	For the three-month period ended March 31		For the year ended December 31
	2006 (Unaudited)	2005 (Unaudited)	2005 (Audited)
	NIS thousands	NIS thousands	NIS thousands
Current assets	**229,579**	250,045*	366,078
Long-term investments and debit balances	**33,509**	26,251*	28,702
Fixed assets	**303,197**	345,015	305,826
Other assets	**22,223**	17,314	23,625
	588, 508	638,625	724,231
Current liabilities	**238,685**	227,377	401,126
Long-term liabilities	**16,643**	182,077	14,835
Shareholders' equity	**333,180**	229,171	308,270
	588,508	638,625	724,231

B. Statement of Operations

	For the three-month period ended March 31		For the year ended December 31
	2006 (Unaudited)	2005 (Unaudited)	2005 (Audited)
	NIS thousands	NIS thousands	NIS thousands
Revenues from international telecommunication services	**244,852**	199,171	816,664
Operating expenses	**160,976**	132,835*	530,806
Gross profit	**83,876**	66,336	285,858
Marketing, general and administrative expenses	**50,728**	45,819*	193,297
Operating income	**33,148**	20,517	92,561
Financing income (expenses), net	**813**	(1,589)	(3,361)
Earnings after financing, net	**33,961**	18,928	89,200
Other expense (income), net	**(206)**	340	1,377
Earnings before income tax	**33,755**	19,268	90,577
Tax benefit (income tax)	**(10,804)**	6,778	15,226
Earnings after income tax	**22,951**	26,046	105,803
Company's equity in earnings of an affiliated company	**1,624**	204	4,583
Net earnings	**24,575**	26,250	110,386

* Reclassified