

EL AL ISRAEL AIRLINES LTD.

FINANCIAL STATEMENTS AS OF SEPTEMBER 30, 2007 (unaudited)

CONTENTS

SECTION A - UPDATE OF CHAPTER A TO 2006 ANNUAL REPORT

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Update of Chapter A (Description of the Corporation's Business)¹
to the Periodic Report for the Year 2006 ("the Periodic Report")
of El Al Israel Airlines Ltd. (hereafter: "the Company")

1. Description of the General Development of the Group's Business

To Item 3.2 – options and Item 9.4.5 – employee compensation plan

- a) Further to the resolution on a dividend distribution, as provided in the Immediate Report dated October 8, 2007 (and also see below), the theoretical exercise price of the options that were allotted to employees pursuant to the outline published on February 27, 2006, as amended on March 15, 2006, and pursuant to the outline published on May 29, 2006, and where not yet exercised, was reduced by the full amount of the gross dividend per share that was distributed.
- b) On November 20, 2007, the Company's board of directors approved publication of an outline for the purpose of allotting options that were returned to the reserve of options that may be allotted pursuant to the terms of the 2006 option plan, from the original quantity as provided in the outline dated February 27, 2006, and as amended on March 15, 2006 and/or from the additional quantity, as provided in the outline dated May 29, 2006, and in total – 3,382,843 options.

Likewise, the board of directors approved the allotment of 2,195,852 options to 6 offerees (including one officer), subject to receiving the required approvals, as well as approval of the Company's board of directors for empowering the Human Resources and Appointments Committee of the board of directors to continue serving as administrator of the 2006 options plan, and to allot options to the Company's managers according to the criteria prescribed by the board of directors. For additional information, see Note 8.3 to the financial statements.

To Item 3.4 and 3.5 – changes in interested party holdings

Further to the update of Item 3.4 as provided in the financial statements as at June 30, 2007, and as the Company reported in its current reports, it should be noted that Tamar Borovitz, Deputy Chairman of the Company's Directorate, directly holds 0.05% of the issued capital.

To Item 4 – dividend distribution

- a) Further to Item 4 of the periodic report, and as the Company reported in its Immediate Report dated October 8, 2007, the Company's board of directors resolved on October 7, 2007, to distribute a dividend of NIS 0.075 per share, totaling NIS 37,178,926, which is 5.98% of issued and paid-up capital.

The dividend distribution was executed on October 29, 2007.

The said distribution differs in substance from the Company's dividend policy, which the Company's board of directors prescribed in December 2005, and was adopted considering that this dividend distribution policy explicitly kept the authority to decide on a distribution in the hands of the board of directors. This decision on a distribution was adopted in view of the Company's liquidity situation and the decrease in the accumulated deficit balance, and in view of the fact that the Company had not distributed a dividend to date.

¹ The update is in accordance with Regulation 39A to the Securities Regulations (Periodic and Immediate Reports), 1970, and includes material changes and developments which took place in the entity's business with regard to every matter which must be described in the Periodic Report. The update makes reference to the numbers of the Sections in Chapter A (Description of the Entity's Business) in the Group's Periodic Report for the year 2006.

- b) On November 30, 2007, the Company's board of directors resolved to update the dividend policy on which it had decided on March 28, 2005. Within the scope of the new dividend policy, the Company will aspire to distribute dividends to its shareholders, at its discretion, and in accordance with the Company's needs, including its liquidity, activities and business plans as they will be from time to time.

To Item 6.3 – Fluctuations in jet fuel prices, and to Item 9.5.1 – Raw materials and suppliers – fuel

In the quarter ended September 30, 2007, market prices of jet fuel increased by an average of 4%, compared with the same quarter last year. The Company's jet fuel expenses increased in the quarter by 9%, after hedging activity, compared with the same period last year. However, the Company's fuel expenses fell from 29.5% in the third quarter of 2006 to 27.2% in the reported quarter.

To Item 6.4 – Fluctuations in inter-currency exchange rates

The Group's results are affected by several currencies. Fluctuations in the exchange rate of the U.S. dollar against other currencies could lead to improvement or erosion in the Group's profitability.

As at September 30, 2007, there was a 6.7% decrease in the exchange rate of the U.S. dollar against the shekel compared with September 30, 2006, a decrease of 5.6% compared with June 30, 2007 and a decrease of 5% compared with December 31, 2006.

As at September 30, 2007, there was a 10.6% decrease in the exchange rate of the U.S. dollar against the euro compared with September 30, 2006, a decrease of 5.2% compared with June 30, 2007 and a decrease of 7.1% compared with December 31, 2006.

For additional information, see Par. 3.4 of the Report of the Board of Directors on the State of the Corporation's Affairs.

To Item 6.5 – Fluctuations in interest rates

For the purpose of financing the purchase of aircrafts, the Company assumed significant loans at variable interest based on the Libor rate (see Par. 9.8.4 of the Periodic Report and its update below). Fluctuations in the Libor interest rate could have a material effect on the Company's financing expenses. For additional information, see Note 3 to the financial statements.

In the third quarter of 2007, the 3-month Libor interest rate increased by an average of 0.2%, compared with its average rate in the third quarter of 2006, and an increase of 1.6% relative to the average rate as in the quarter ended June 30, 2007.

For additional information, see Par. 6.3 of the Report of the Board of Directors on the State of the Corporation's Affairs.

2. Passenger Aircraft Area

To Item 7.1.3(A) – Developments in volume of international activity

According to IATA reports, in the months January-September 2007, there was an increase of 7.3% in international passenger traffic relative to the same period last year, i.e. a higher growth rate than the annual rate expected in IATA's estimates (5%).

To Item 6.2 – Traffic in the Israel aviation industry and to Item 7.3.1(B) Developments in the volume of activity in the Israeli market

According to the data of the Central Bureau of Statistics, in the months July-September 2007, there was an increase of 53% in the number of inbound tourists traveling to Israel by air, compared with the same quarter last year, and an increase of 15% in the number of outbound Israelis traveling by air, compared with the same quarter last year. In total, the traffic in Ben-Gurion Airport grew by 25.5% compared with the same quarter last year. The increase in this quarter is explained mainly against the backdrop of the decrease in traffic in the third quarter last year due to the Second Lebanon War, and by the fact that the holiday season, in which there is generally an increase in traffic, occurred in September 2007, whereas in 2006, the holiday season was mostly in the month of October.

In total, the growth in passenger traffic in Ben-Gurion Airport in the period between January-September 2007 was 14.1% compared with the same period last year, i.e. a higher growth rate than that projected by IATA estimates (5.1%).

To Item 7.1.4 – Developments in the markets of the areas of activity, Item 7.1.8 – Main entry and exit barriers of the area of activity and changes occurring therein, Item 7.1.10 – Competitive structure in areas of activity and changes therein, Item 9.11.7.2 – Designated carrier, Item 9.11.7.3 – Ownership and control of designated carrier, Item 9.11.7.4 – Capacity, 9.11.7 – Aviation agreements and civil and international aviation policy of Israel, 9.18.3 – Discussion of risk factors: changes in competition and Item 9.18.12 – Discussion of risk factors: Effect of activity of Low Cost companies on the Israeli market

Further to the updates provided in the financial statements as at March 31, 2007 and June 30, 2007:

A) In the new aviation agreement between Israel and Britain signed in September 2007, it was agreed that each country would be able to appoint two scheduled designated carriers for each city pair. Likewise, it was agreed that each party could appoint a carrier, the principle place of business of which was found in the territory of the appointing party, and which holds an air operator's license that was issued by the appointing party. In conversations, it was also agreed that the Luton Airport in western London will not be included in the airport system of London for the purpose of appointing designated carriers for this destination.

As a result of this agreement:

- 1) The British company, "Thomsonfly", a low cost company of the TUI Group (German-owned), filed a request with the Israel Civil Aviation Authority to operate scheduled flights in the 07/08 winter season on the Luton – Tel Aviv route and the Manchester – Tel Aviv route. Thomsonfly commenced operation of flights on these routes in November 2007.
- 2) British Midland Airlines (BMI) received the status of the second designated British carrier for the London – Tel Aviv route, and according to reports, plans to operate a daily flight on the route commencing April 2008.

- 3) Israir requested to be appointed the second designated Israeli carrier on the Tel-Aviv – London route. Regarding the terms of the appointment of a designated carrier in addition to the Company, see Item 9.11.7.2 of the Periodic Report.
- B) At the Company's request, in August 2007, the Minister of Transportation appointed the Company a designated carrier on the Japan route. The Company began checking out the possibilities of using this right.
- C) In aviation discussions held between Israel and Russia, it was agreed that on the Tel-Aviv – Moscow route, each country would be able to appoint an additional designated carrier for passengers and/or cargo, as a temporary arrangement for a period of up to two years. Likewise, it was agreed to increase the weekly frequency that can be operated on the route. Regarding charters, it was agreed that each party could appoint up to two carriers and to increase the weekly frequency. Likewise, the flight framework – scheduled and charters – allowed on the Tel-Aviv – Saint Petersburg route was expanded. Regarding the terms for appointment of a designated Israeli carrier in addition to the Company, see Item 9.11.7.2 of the Periodic Report.
- D) Further to the update included in the financial statements as at March 31, 2007, regarding agreements between Israel and France, it should be noted that the French company "New Axis", which until now has operated charter flights on the Tel-Aviv – Marseilles route, announced its intention to begin to operate scheduled flights on the route as from December 2007.
- E) Lufthansa is working to resume operation of its flights on the Munich – Tel-Aviv route commencing in spring 2008, in addition to the daily flights it now operates on the Frankfurt route.
- F) In October 2007, the Group submitted a request to the Civil Aviation Authority for its appointment as the designated carrier on domestic routes.

To Item 7.1.5 – Technological changes

- A) Further to the details in the Periodic Report related to the ERP Project, it should be noted that the Company's board of directors approved an undertaking with IBM as head integrator for application of the back office system, using the ERP technology of SAP and Ramco (for maintenance and engineering).
- B) Further to the details in the Periodic Report related to the replacement of the Carmel Reservations System, it should be noted that in August, the Company signed an agreement with Amadeus, and began preparations for replacing the system and customizing the interface systems.

To Item 7.1.10(D) – Competitive structure in the area of activity and changes therein – charter companies

In the third quarter of 2007, an increase of 81% was posted in the foreign charter traffic in BGA compared with the same quarter last year, due mainly to the decrease in traffic in the third quarter last year, due to the Second Lebanon War and to the holiday season in 2007 occurring mainly in September, whereas in 2006, the holidays occurred mainly in October, and to discontinuation of the activities of the Company and of the Israeli charter companies on the Turkish routes, against the backdrop of the high security costs borne by the Israeli companies.

To Item 7.2(B) – Services in the area of activity – data relating to the Groups categories of destinations

Further to the information provided in the table in Item 7.2 (B) of the Periodic Report, related to the Company's assessments of the Group's market share in Ben Gurion Airport, it should be noted that the Group's assessment, subject to the parenthetical comments 20 in the Periodic Report, in the third quarter of 2007, the Group's total market share in Ben Gurion Airport was 34.6%, compared with 38.6% in the same quarter last year, i.e. a decrease of 10.6%. A considerable part of the decrease was caused by the sizable increase in passenger traffic on the routes to Turkey, which account for 15% of total passenger traffic in Ben Gurion Airport, and by the discontinuation of the activity of the Group (and of the other Israeli airlines) on routes to Turkey, due to the high security costs borne by the Israeli companies.

To Item 7.2(F) – Other routes

In the "Other Routes" (Turkey, Greece, Cyprus, South Africa and Egypt), there was growth of 58% in passenger traffic in the third quarter, compared with the same quarter last year, mainly against the backdrop of the decrease in traffic that occurred in the third quarter last year, due to the Second Lebanon War, and to the holiday season in 2007 occurring mainly in September, whereas in 2006, the holidays occurred mainly in October. Most of the increase was posted on the routes to Turkey, in which the passenger traffic grew by 74% compared with the same quarter last year.

As a result of the discontinuation of flights to destinations in Turkey by Israeli airlines because of the high security costs, there was a 47% increase in the activity of Turkish Airlines to Israel and a 156% increase in the activity of Turkish charter companies to Israel in the third quarter of 2007.

To Item 7.10 – Production capacity

In the third quarter of 2007, the average load factor in the Company's passenger planes stood at 87%, compared with 80.7% in the same quarter last year, i.e. improvement of 7.8%.

To Item 7.11 – Passenger aircraft fleet

In addition to the information in Item 7.11.1 of the Periodic Report, and the update as provided in the financial statements as at March 31, 2007, it should be noted that:

- A) At the end of August 2007, the Company received possession of the second of two new Boeing 777-200 ER aircraft that it had purchased from Boeing. In the Group's service, the aircraft will contain 279 seats, including bed-seats (that can recline to a prone or almost prone position) in the premium classes as well as new entertainment systems and a new design.
- B) As part of the Company's business strategy to gradually refresh its aircraft fleet, in August 2007, the Company's board of directors approved the conversion of the Company's fleet of Boeing 757-200 planes to Boeing model 737-800 planes, based on the availability and specific terms of the transaction. The Company is attempting to identify opportunities, as noted.
- C) A 757-200 plane, for which the lease expired in October 2007, as noted in the table in Item 7.11 B) of the Periodic Report, was returned to its owners.
- D) On November 2007, the Company's board of directors approved the purchase of a Boeing model 747-400 plane manufactured in 1994, designated for the Company's use not later than November 2008, and when in the Company's service, will contain 395 seats. The estimated investment needed to purchase the plane, including the investments needed by the Company to take in the plane, subject to completion of the negotiations for the purchase and decisions regarding the scope of the additions and installations to be made in the plane to tailor it to the Company's needs, is estimated at \$50 million. The independent financing is expected to total \$10 million, and the balance will be financed by loans.

3. Cargo aircraft segment

To Item 6.1 – Traffic in the international aviation industry and Item 8.1.3(A) – International developments in the volume of activity and profitability of the segment

According to IATA reports, in the months January – September 2007, there was an increase of 4% in the volume of global transport of cargo in cargo planes compared with the same period in 2006 – i.e. growth at a lower rate than the annual rate projected by IATA (5.3%). The halt in the growth was due to the high fuel prices and competition from alternative means of transportation, especially shipping by sea. Nonetheless, it is not possible to estimate whether this data changes expectations regarding the total annual growth rate for 2007.

To Item 8.5 – Customers, marketing and distribution

Further to the information provided in Item 8.5 to the Periodic Report related to interested party and director of the Company that purchased ownership in a cargo agency with which the Company has business ties, it should be noted that the aforementioned stopped serving as a director in the Company.

To Item 8.7.1 – Competitive conditions in the area of activity

- A) Further to the information provided in Item 8.7.1B of the Periodic Report, it should be noted that in August 2007, the Minister of Transportation appointed the Company the designated carrier for the route to Japan, also for the purpose of operating cargo flights. The Company has begun to check out the possibility of using these rights.
- B) Further to the information provided in Item 8.7.1.C of the Periodic Report, it should be noted in aviation discussions held between Israel and Russia, it was agreed that on the Tel-Aviv – Moscow route, each company may appoint an additional scheduled carrier for passengers and/or cargo, as a temporary arrangement for a period of up to two years. Likewise, it was agreed to increase the weekly frequency that may be operated on the route. With respect to charter flights, it was agreed that either party may appoint up to two carriers, and to increase the weekly frequency. Likewise, the flight framework allowed on the Tel-Aviv – Saint Petersburg route – scheduled and charter – would be expanded. To the best of the Company's knowledge, CAL has requested to be appointed the second designated carrier of Israel for operating cargo flights.
- C) Further to the information provided in Item 8.7.1D of the Periodic Report, it should be noted that to the best of the Company's knowledge, the Korean airline has submitted a request with the Civil Aviation Authority, to extend the approval to make weekly flights to Seoul also in the 2007/2008 winter season.
- D) Further to the information provided in Item 8.7.1E and at the end of Item 8.2 of the Periodic Report, it should be noted that the Group estimates that its share in cargo transport in the period between January-September 2007, out of the total cargo transported by air to and from Israel (including cargo transported in the underbelly of passenger planes, including mail operations and excluding Sixth Freedom) stood at 38.6%.

4. Information on the two operating segments

To Item 9.4.1 – Organizational structure, to Item 9.4.2 – Employed workers and to Item 9.4.16 – Officers and senior executives

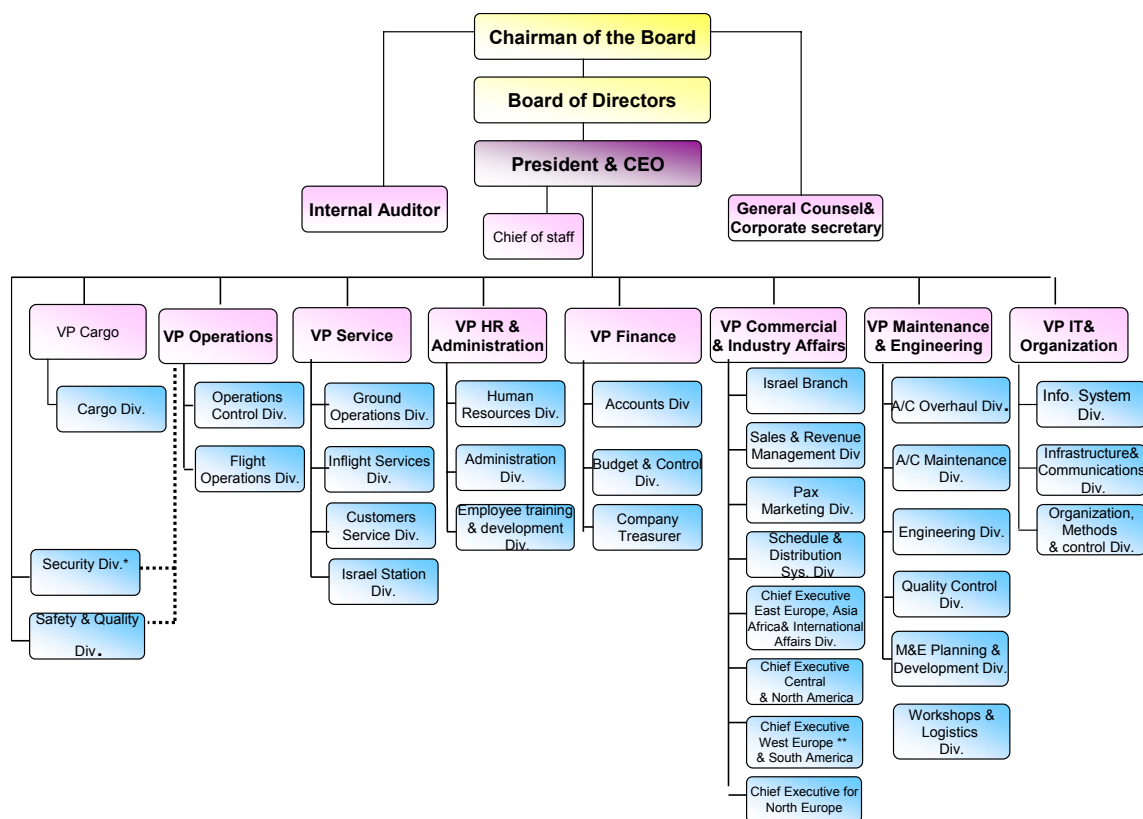
Further to the information in the aforementioned Items of the Periodic Report, and the updates to these Items, as provided in the financial statements as at March 31, 2007 and June 30, 2007:

- In September 2007, a cargo division was created reporting to the VP Cargo.
- In September 2007, the planning and development, maintenance and engineering sub-division was converted to a division, reporting to the VP Maintenance and Engineering.
- In October 2007, the aircraft overhaul and logistics division was split into two divisions - the aircraft overhaul division and the workshops and logistics division, both reporting to the VP of Maintenance and Engineering.

As a result of the above organizational changes, the number of members of executive management and other senior employees, as mentioned in the table in Item 9.4.16 of the Periodic Report, was updated to 32 (excluding the Chief Executive Officer).

It should be noted that the Projects, Organizations and Methods Division was renamed the Organizations and Methods and Controls, and the head of the Northern Europe Region Division was renamed EI AI Manager for Northern Europe Region.

Presented below is a flowchart depicting the Company's updated organizational structure:



*Security Div. Mgr. and Safety & Quality Div. Mgr. are subordinated to the CEO and coordinated by VP Operations

To Item 9.4.8 – Pension arrangements – deficit with respect to severance pay and its coverage

Further to the information in Item 9.4.8 of the Periodic Report and updates of this item as provided in the financial statements as at March 31, 2007 and June 30, 2007, it should be noted that since January 1, 2007 through September 30, 2007, deposits were made in the severance pay fund of eligible employees (in thousands of dollars): deposits by the State totaling NIS 104,624,444, deposits by the Company totaling NIS 100,862,605. In total deposits of NIS 205,487,049 were made in the severance pay funds of eligible employees during the said period. After these deposits were made by the Company and the State, the deficit in the fund for eligible employees, as defined in the agreement between the Company, the State and the employee representatives, as signed on the eve of the Company's privatization, were covered in full.

To Item 9.6.5 – Working capital deficit

Refer to the updates in Item 2 of the Report of the Board of Directors on the State of the Corporation's Affairs.

To Item 9.8.1 – Loans for undesignated use and to Item 9.8.4 – Loans for designated use

Further to the information in Par. 9.8.4 in the Periodic Report pertaining to the guarantee of the U.S. Export-Import Bank (Ex-Im) regarding the purchase of two Boeing 777 aircrafts, and the update of this Item in the financial statements as at June 30, 2007, it should be noted that for the second plane, which was delivered to the Company in August 2007, the Company received a \$110 million loan, of which \$88 million is earmarked to pay the balance of the cost to Boeing and the expenses related to obtaining the financing, the balance of \$22 million was returned to the Company. For additional information on the purchase of two Boeing 777 planes, see Item 7.11(a) of the Periodic Report and its update above, and Note 3 below in the financial statements.

To Item 9.8.3 – Credit facilities

The Company's credit facility from banks totaled \$87.5 million as at September 30, 2007, an increase of 39% over the approved facility as at September 30, 2006. The credit facilities are for a time period of up to one year and at variable interest.

To Item 9.11.12 – Security arrangements

Further to the information in Item 9.11.12 of the Periodic Report and the update of this Item as provided in the financial statements as at March 31, 2007 related to the Government's decision to provide financial support to assist in maintaining orderly aviation ties with neighboring countries, it should be noted that the Group approached the Ministry of Transportation with a request for full financing of the cost of securing the flight route to Cairo in 2008, although no response has been received.

To Item 9.14 – Legal proceedings

A) Further to the information in Item 9.14.3 of the Periodic Report, it should be noted that in a deliberation held in the Supreme Court in October 2007, the appeal filed by the plaintiffs of the District Court's ruling, whereby the motion against the Company for recognition as a class action was rejected and the claim was dismissed for lack of cause.

- B) Further to the information in Item 9.14.4 of the Periodic Report, it should be noted that in September 2007, Tel Aviv District Court issued a ruling dismissing the motion against the Company for recognition as a class action. The plaintiffs filed an appeal of the ruling with the Supreme Court.
- C) In November 2007, a claim was filed against the Company in Haifa District Court, as well as a motion for class action recognition under the Class Action Law, in the amount of NIS 105 million (\$26 million). The plaintiffs claim that the prices charged by the Company for overweight baggage on its flights are excessive and calculated without connection to the prices of the Company's ordinary flights. The Company is studying the claim and is preparing its response.

EI Al Israel Airlines Ltd.
Report of the Board of Directors on the State of the Corporation's Affairs
For the Period Ended September 30, 2007

We hereby present the Report of the Board of Directors on the State of the Corporation's Affairs for the period ended on September 30, 2007.

EI Al Israel Airlines Ltd. ("The Company") closed the three months ended September 30, 2007 with net income of \$41.2 million, compared with income of \$1.4 million in the same period last year, during which the Second Lebanon War began.

The Company's sales turnover in the third quarter of the year increased by 27% over the same quarter last year, reaching a record \$567 million.

Gross profit in the third quarter of the year totaled \$151.3 million, 27% of turnover, whereas in the same quarter last year, it totaled \$77.3 million, 17% of turnover.

Net cash provided by operating activities in the third quarter of the year totaled \$74.1 million, and the balance of cash and short-term investments as at September 30, 2007 totaled \$272.7 million.

In the first nine months of 2007, net income totaled \$40.2 million, compared with a loss of \$18.0 million in the same period last year, and net cash provided by operating activities totaled \$178.1 million.

Shareholders' equity as at September 30, 2007 totaled \$312.7 million, compared with \$214.1 million as at December 31, 2006.

In the third quarter of 2007, added to the Company's passenger fleet were two wide-body Boeing 777-200 planes, in which new-model seats and sophisticated entertainment systems are installed, at a total investment of \$250 million, as part of the "EI Al 2010" strategy.

<p>The financial statements as at December 31, 2006 and for the year then ended and as at September 30, 2006 and for the periods of nine months and three months then ended were restated due to the first-time application of Accounting Standard No. 27 – Fixed Assets, and due to a correction of the deferred tax liability – see Note 1.5 to the interim financial statements.</p>

1. The Company and its business environment

1.1 General

The Company serves as the designated air carrier of the State of Israel on most of the international routes operating to and from Israel.

The key activities of the Company and its subsidiaries are the transport of passengers and cargo, including baggage and mail, through scheduled flights, and regarding the transport of passengers, also on charter flights between Israel and overseas. The Company is also engaged in the leasing of flight equipment, in providing maintenance services in its home airport, in the sale of duty-free products, and through investees – in ancillary activities, mainly the manufacture and supply of airline food and the management of several travel agencies.

The business environment in which the Company operates is the international civil aviation industry, and inbound and outbound tourism, which is characterized by a seasonal nature and strong competition. This competition intensified during 2006, mainly as a result of the growth in operations of foreign airlines, which significantly increased the capacity of passengers to and from Israel by adding frequency and/or the use of larger planes on the route. This trend also continued in 2007.

The Group has two operating segments:

- A) **Air transport in passenger planes** - In this segment, the Group transports passengers, as well as cargo (including mail and baggage) in the underbelly of passenger planes, and provides ancillary services, such as: the sale of duty-free products and the leasing of passenger plans.
- B) **Air transport in cargo planes** – In this segment, the Group transports cargo in cargo planes and also provides ancillary services.

1.2 Privatization of the Company

By June 5, 2007, all of the call options (Series B) were exercised, for a total of 157,600,000 options. As a result of the exercise of the call options (Series B), the State's holdings in the issued and paid-up capital of the Company fell to 1.1% on June 5, 2007.

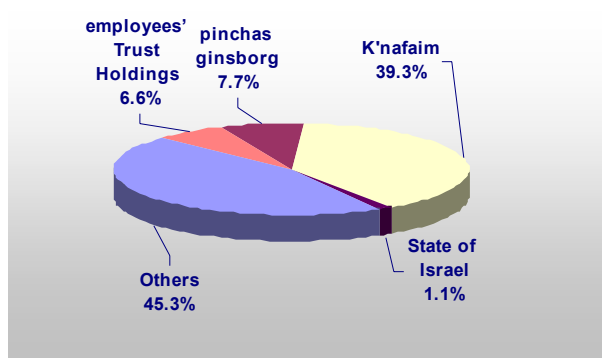
Additionally, by June 5, 2007, 99,998,588 options (Series 1) out of 100,000,000 options were exercised. The balance of unexercised options (Series 1) as at June 5, 2007 (1,412 options) expired, and are null and void.

As at September 30, 2007, the holdings in the Company were:

Knafaim Holdings Ltd. ("Knafaim") – 39.3%, Pinchas Ginsburg – 7.7%, employee corporation, "Holdings in Trust of El Al Employees Ltd. ("Employees Corporation") – 6.6%, State of Israel – 1.1%, others – 45.3%.

For additional information related to the Company's privatization, see Note 1.B to the Periodic Report as at December 31, 2006.

**Shareholdings in Company
at September 30, 2007 (undiluted):**



2. Financial position (consolidated financial statements)

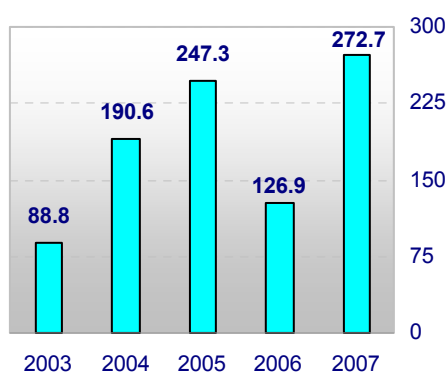
	30.09.2007	31.12.2006 *	Change	
	In thousands of dollars	In thousands of dollars	In thousands of dollars	%
Assets				
Cash and short-term investments	272,708	150,840	121,868	81%
Trade accounts receivable	171,409	132,544	38,865	29%
Receivables and other current assets	58,825	47,342	11,483	24%
Deferred income taxes	7,831	30,645	(22,814)	(74%)
Inventory	15,095	17,190	(2,095)	(12%)
Investments	6,281	5,945	336	6%
Fixed assets	1,293,818	1,176,528	117,290	10%
Other assets	3,626	3,455	171	5%
	1,829,593	1,564,489	265,104	17%
Liabilities & Equity				
Short-term borrowings and current maturities	65,451	105,100	(39,649)	(38%)
Trade accounts payable	182,653	144,990	37,663	26%
Payables and other current liabilities	402,107	332,691	69,416	21%
Long-term loans from financial institutions	736,191	566,104	170,087	30%
Accrued severance pay, net	68,632	126,171	(57,539)	(46%)
Deferred income taxes	61,369	74,603	(13,234)	(18%)
Other long-term liabilities	473	730	(257)	(35%)
Shareholders' equity	312,717	214,100	98,617	46%
	1,829,593	1,564,489	265,104	17%

* Restated – see Note 1.3.1 and Note 1.5 to the interim financial statements.

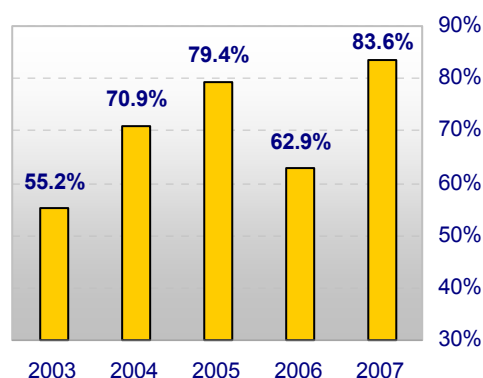
2.1 The main changes in asset, liability and shareholders' equity items as at September 30, 2007 compared with December 31, 2006 are:

- Increase in cash and short-term investments, due mainly to the positive cash flows from operating activities in the current period and to loans received, offset by investments in fixed assets and the repayment of loans.
- Increase in trade accounts receivable, due mainly to growth in passenger sales as a result of seasonal changes.
- Growth in receivables and other current assets, due mainly to the increase in prepaid commissions, due to the increase in passenger sales.
- Increase in fixed assets, due mainly to investment in the purchase of two new Boeing model 777-200 planes received in the current period, offset by periodic depreciation expenses in the current period.
- Increase in trade accounts payable, due to the growth in activity, resulting from seasonal changes.
- Increase in payables and other current liabilities, due mainly to the increase in prepaid income, as a result of the increase in sales of not yet utilized air tickets.
- Increase in the balance of long-term loans (including current maturities) as a result of the receipt of loans to finance the two new model 777-200 passenger planes, offset by current repayments of long-term loans.
- Decrease in accrued severance pay, net, due mainly to the deposits made by the Company and the State in the severance pay fund, as a result of the exercise of the call options (Series B) of the State and of options (Series 1) of the Company.
- Increase in net deferred tax liability deriving from tax expenses recorded by the Company in the current period.
- Increase in the Company's shareholders' equity, due mainly to the income in the current period and to the exercise of options (Series 1) issued by the Company, which led to an increase in share capital and premium on shares, as well as to the deposits by the State of Israel in the severance pay fund, which led to an increase in the capital reserve from transactions with a former controlling owner.

Cash and cash equivalents and short-term investments
At September 30 (in \$ millions)



Current ratio by % - at September 30 :



As at September 30, 2007, the Company has a working capital deficit of \$124.3 million, compared with a deficit of \$204.2 million as at December 31, 2006. The Company's current ratio as at September 30, 2007 is 80.9%, compared with 65.0% as at December 31, 2006.

The decrease in the working capital deficit is due to the increase in cash balances and short-term investments, and to the increase in trade accounts receivable and other assets, and to the decrease in the current maturities of long-term loans, resulting mainly from the payment of a loan to an Israeli bank, offset by the increase in prepaid income from the sale of not yet utilized air tickets and in the balance of trade accounts payable.

The working capital deficit is due to the Company's current liabilities, which contain two significant elements: prepaid income from the sale of airline tickets and the current maturities of long-term loans. These elements, which are characterized by a cyclical nature, are included in current liabilities, and essentially explain most of the working capital deficit.

2.2 First-time application of Accounting Standard No. 27 – Fixed Assets

Commencing January 1, 2007, Accounting Standard No. 27 – Fixed Assets, took effect, providing the accounting treatment for fixed assets.

The Company's management decided to institute the accounting policy of measuring fixed assets by the cost method, as was its practice before publication of the Standard.

Regarding the provisions of the Standard and the restatement of the financial statements as at December 31, 2006 and as at September 30, 2006, as a result of application of the Standard – see Note 1.3.1 and Note 1.5 to the interim financial statements.

3. Analysis of operating business results of EI AI

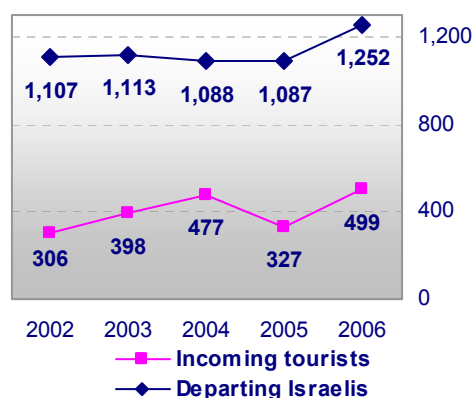
3.1 Market data

Passenger and cargo traffic at BGA	2007 in thousands	2006 in thousands	change in thousands	%
Jul - Sep				
Incoming tourists *	499	327	172	53%
Departing Israelis *	1,252	1,087	165	15%
Cargo import - tons **	35	35	(0)	(0%)
Cargo export - tons **	42	40	2	6%
Jan - Sep				
Incoming tourists *	1,318	1,220	98	8%
Departing Israelis *	2,731	2,450	281	11%
Cargo import - tons **	102	101	1	1%
Cargo export - tons **	143	137	6	5%

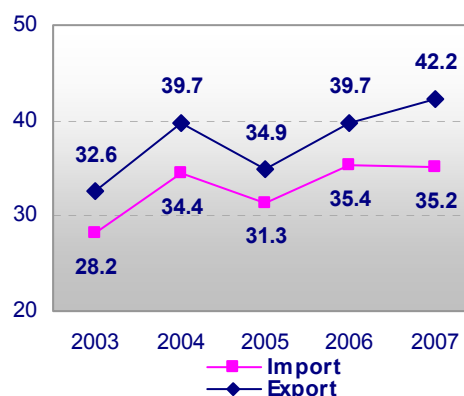
* Source: Central Bureau of Statistics.

** Does not include cargo in transit.

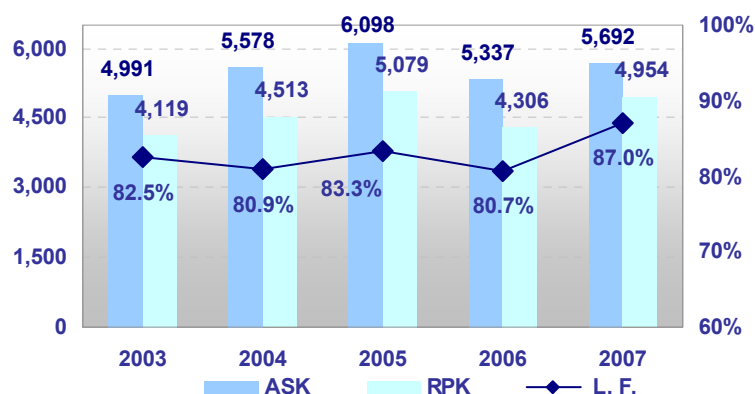
Passenger traffic at BGA
Incoming tourists & departing Israelis,
third quarter by year:
(In thousands)



Import & Export of cargo by air from / to Israel, third quarter by year: (In thousands tons)



Operating data in the third quarter, by year: (in millions)



3.2 Company operating data

	July - September 2007	July - September 2006	Change
Passenger legs (scheduled and chartered) (paying passengers) - in thousands	1,149	1,014	13%
RPK (scheduled) - in millions	4,954	4,306	15%
ASK (scheduled) - in millions	5,692	5,337	7%
Load factor (scheduled)	87.0%	80.7%	8%
Company's market share (scheduled and chartered)	35.1%	39.1%	(10%)
Flown cargo, in thousand tons	37	34	9%
RTK - in millions	216	199	9%
Weighted flying hours (including leased equipment) - in thousands(*)	48	45	7%
<u>Average man-years (EI AI only):</u>			
Permanent	3,544	3,707	(4%)
Temporary	2,660	2,650	0%
Total	6,204	6,357	(2%)

	January - September 2007	January - September 2006	Change
Passenger legs (scheduled and chartered) (paying passengers) - in thousands	2,828	2,757	3%
RPK (scheduled) - in millions	12,834	12,262	5%
ASK (scheduled) - in millions	15,008	15,124	(1%)
Load factor (scheduled)	85.5%	81.1%	5%
Company's market share (scheduled and chartered)	37.4%	41.6%	(10%)
Flown cargo, in thousand tons	113	119	(5%)
RTK - in millions	623	639	(2%)
Weighted flying hours (including leased equipment) - in thousands(*)	128	130	(2%)
<u>Average man-years (EI AI only):</u>			
Permanent	3,546	3,701	(4%)
Temporary	2,394	2,548	(6%)
Total	5,940	6,249	(5%)
Aircraft in operation - end of period - number of units	37	34	3
Average age of owned fleet at end of period - in years	14.5	14.6	(0.1)

Glossary:

Passenger leg – Flight coupon in one direction.

RPK – Revenue Passenger Kilometer – number of paying passengers multiplied by distance flown.

ASK – Available Seat Kilometer – number of seats offered for sale multiplied by distance flown.

RTK – Revenue Ton Kilometer – weight of paid flown cargo in tons multiplied by distance flown.

Passenger Load Factor (occupancy) – flown passenger-km is expressed as a percentage of available seat-km.

* Weighted flight hours in terms of Boeing 767/757.

Weighted value of the planes: Boeing 767/757 = 1.0; Boeing 747 = 2.0; Boeing 777 = 1.6; Boeing 737 = 0.6.

These weighted values were determined based on an estimate of the total expenses of each type of aircraft, and are used consistently to calculate weighted flight hours as an indicator of the volume of aviation activity.

3.3 Statement of operations data

For the three-month period ended September 30, 2007 (consolidated financial statements):

	July - September 2007		July - September * 2006		<u>change</u>	
	in thousands of dollars	% of operating revenues	in thousands of dollars	% of operating revenues	in thousands of dollars	%
Operating revenues	566,715	100%	447,001	100%	119,714	27%
Operating expenses	(415,739)	(73.3%)	(369,690)	(82.7%)	(45,689)	12%
Gross profit	151,336	26.7%	77,311	17.3%	74,025	96%
Selling expenses	(65,904)	(11.6%)	(46,673)	(10.4%)	(19,231)	41%
General and administrative expenses	(21,588)	(3.8%)	(22,116)	(4.9%)	528	(2%)
Operating income before financing	63,844	11.3%	8,522	1.9%	55,322	649%
Financing expenses ,net	(10,386)	(1.8%)	(6,725)	(1.5%)	(3,661)	54%
Other expenses, net	(2,445)	(0.4%)	(241)	(0.1%)	(2,204)	915%
Income before taxes on income	51,013	9.0%	1,556	0.3%	49,457	3178%
Income tax expenses	(9,914)	(1.7%)	(180)	(0.0%)	(9,734)	5408%
Income after taxes on income	41,099	7.3%	1,376	(0.3%)	39,723	2887%
Company's equity in results of affiliates, net	54	0.0	34	0.0%	20	59%
Net income for the period	41,153	7.3%	1,410	0.3%	39,743	2819%

* Restated – see Note 1.3.1 and Note 1.5 to the interim financial statements.

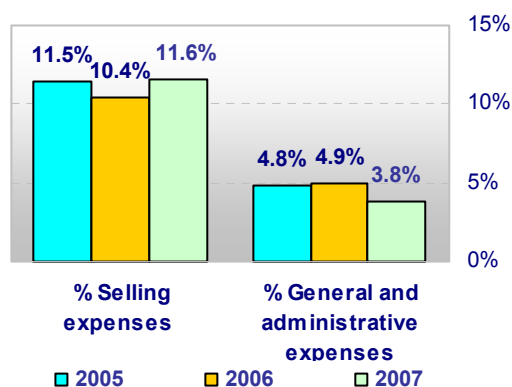
The key factors that influenced the business results in the three-month period ended September 30, 2007 compared with the same period last year are:

- The increase in operating revenues is due mainly to the increase in passenger revenues, compared with the same period last year, in which the Second Lebanon War occurred, as a result of the 15% increase in RPK flown by the Company and an increase in revenue per RPK. Additionally, there was an increase in cargo revenues, due to the increase in activity, in revenues from aircraft leasing and from the maintenance services provided to other airlines.
- In the third quarter of 2007, there was an increase in the Company's operating expenses compared with the same period last year, due mainly to the increase in jet fuel expenses, as described below, and in most operating expenses, due mainly to the increase in activity in the quarter and the devaluation of the dollar relative to the shekel and the euro. The increase in salary expenses was also due mainly to the increase in activity during the quarter and to the devaluation of the dollar relative to the shekel. Regarding the effect of the changes in the exchange rates of the shekel against the dollar on the Company's provisions, see Par. 3.4 below. The rate of increase in operating expenses is lower than the rate of increase in revenues, mainly as a result of the operating efficiency measures instituted, as expressed in the improved load factors in passenger aircrafts, from 80.7% in the same quarter last year to 87.0% in the reported quarter.
- The Company's expenses for jet fuel rose in the third quarter of 2007 to \$154.4 million, after payments received for hedging totaling \$5.1 million, compared with the same quarter last year, in which they totaled \$131.9 million (after receiving payments for hedging of \$17.5 million). The increase in fuel expenses was due to the increase in activity compared with the same period last year and to the increase in the effective price to the Company. Jet fuel expenses in the reported

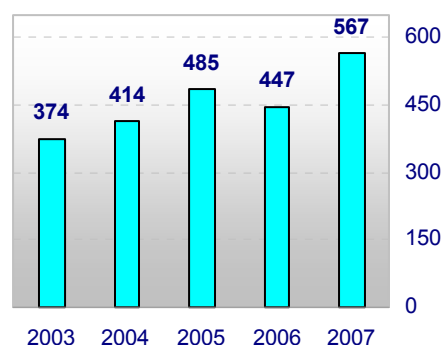
quarter account for 27.2% of the Company's turnover, compared with 29.5% in the same quarter last year.

- Selling expenses increased mainly as a result of the growth in passenger sales and in the rate of distribution expenses.
- The general and administrative expenses decreased as a result of the continuation of the efficiency and savings measures instituted by the Company, and their total percentage of turnover fell from 4.9% in the same quarter last year to 3.8% in the reported quarter.

Selling expenses & general and administrative expenses as % of turnover, in the third quarter by year:



Operating income for the third quarter by year (in millions of dollars):



- The growth in financing expenses resulted mainly from the increase in loans and from the appreciation of the shekel against the dollar at a higher rate than the appreciation that occurred in the same quarter last year, which were offset by the increase in interest income on deposits.
- In the current period, the Company recorded other expenses, net, of \$2.4 million, due mainly to effect of the appreciation of the shekel on liabilities for the early retirement plan, compared with other expenses, net, of \$0.2 million in the same quarter last year.
- In the third quarter of 2007, income tax expenses of \$9.9 million were recorded, compared with expenses of \$0.2 million in the same quarter last year, due to the increase that occurred in the Company's taxable income.

Statement of operations data

For the nine-month period ended September 30, 2007 (consolidated):

	<u>January-September</u> 2007		<u>January-September</u> * 2006		<u>change</u>	
	in thousands of dollars	% of operating revenues	in thousands of dollars	% of operating revenues	in thousands of dollars	%
Operating revenues	1,408,156	100%	1,248,750	100%	159,406	13%
Operating expenses	(1,110,380)	(78.9%)	(1,044,846)	(83.7%)	(65,534)	6%
Gross profit	297,776	21.1%	203,904	16.3%	93,872	46%
Selling expenses	(159,365)	(11.3%)	(135,714)	(10.9%)	(23,651)	17%
General and administrative expenses	(65,965)	(4.7%)	(67,640)	(5.4%)	1,675	(2%)
Operating income before financing expenses	72,446	5.1%	550	0.0%	71,896	13072%
Financing expenses, net	(27,035)	(1.9%)	(21,860)	(1.8%)	(5,175)	24%
Other income (expenses), net	4,174	0.3%	(1,518)	(0.1%)	5,692	
Income before taxes on income	49,585	3.5%	(22,828)	(1.8%)	72,413	
Income tax savings (tax expenses)	(9,580)	(0.7%)	4,719	0.4%	(14,299)	
Income (loss) after taxes on income	40,005	2.8%	(18,109)	(1.5%)	58,114	
Company's equity in results of affiliates, net	145	0.0%	129	0.0%	16	12%
Net income (loss) for the period	40,150	2.9%	(17,980)	(1.4%)	58,130	

* Restated - see Note 1.3.1 and Note 1.5 to the interim financial statements.

The key factors that influenced the business results in the nine-month period ended September 30, 2007 compared with the same period last year are:

- The increase in operating revenues is due mainly to the increase in passenger revenues and to the increase in other income, such as the sale of duty-free items, the leasing of aircraft and maintenance services provided to outside parties, which were offset in part by the decrease in cargo revenues.
- In the first nine months of 2007, there was an increase in the Company's operating expenses compared with the same period last year, due mainly to the increase in jet fuel expenses and the increase in other operating expenses, due mainly to the increase in the number of passengers flown by the Company and to the devaluation of the dollar relative to other currencies. However, it should be noted that operating expenses as a percentage of turnover decreased from 83.7% in the first nine months of 2006 to 78.9% in the first nine months of 2007, mainly as a result of the operating efficiency measures instituted, as expressed in the improved load factors in passenger aircrafts, from 81.1% in the same period last year to 85.5% in the reported period.

Salary expenses in the first nine months of 2007 remained without significant change compared with the same period last year (devaluation of the dollar relative to the shekel and the euro increased the salary expenses, while the decrease in the number of employees and the operating efficiency reduced salary expenses). Their percentage of turnover in the reported period decreased compared with the percentage of turnover in the same period last year.

Regarding the effect of the changes in the shekel/dollar exchange rate on the Company's provisions, see Par. 3.4 below.

- The Company's expenses for jet fuel in the first nine months of 2007 increased compared with the same period in 2006, from \$346.5 million to \$389.1 million, after receiving payments for hedging of \$1.7 million in the first nine months of 2007 (compared with received payments for hedging

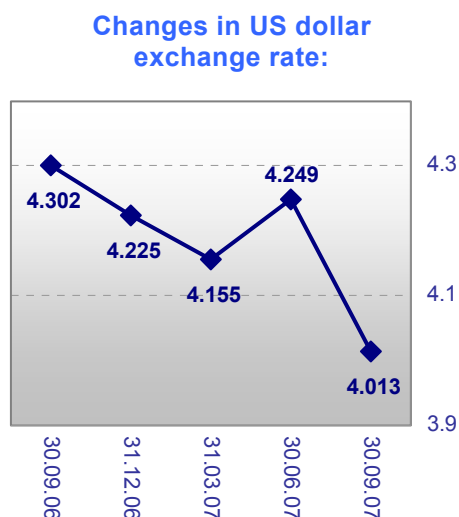
totaling \$52.0 million in the same period last year). The increase in fuel expenses was due to the increase in the effective price to the Company. Jet fuel expenses in the first nine months of 2007 remained without significant change compared with the same period last year (27.6% of turnover).

- Selling expenses in the first nine months of 2007 increased, mainly as a result of the increase in passenger sales and in the rate of distribution commissions.
- The administrative and general expenses decreased as a result of the efficiency and savings measures instituted by the Company and their percentage of turnover in the reported period is lower than the rate in the same period last year.
- The growth in financing expenses in the first nine months of 2007 resulted mainly from the increase in loans and from the increase in the average interest, which was offset by financing income on the Company's deposits, mainly as a result of the increase in deposit amounts.
- In the first nine months of 2007, income tax expenses of \$9.6 million were recorded, compared with tax savings of \$ 4.7 million in the same period last year, due to the increase that occurred in the Company's taxable income in the current period, compared with a tax loss in the same period last year.
- In the current period, the Company recorded other income, net, of \$4.2 million, compared with other expenses, net, of \$1.5 million in the first nine months of 2006. Most of the income in the current period is due to refunds received from Boeing related to the overall accounting between the parties, as well as from vacating a property used by the Company in Heathrow Airport in London. On the other hand, an expense of \$8 million was recorded in the first nine months of 2007 for additional early retirement plans.

3.4 Effect of changes in the exchange rate on the Company's accrued severance pay liability (including early retirement plans) and on the provision for vacation and sick pay ("effect of changes in exchange rate on Company provisions")

In the three-month period ended September 30, 2007, the exchange rate of the shekel appreciated against the dollar by 5.6%, compared with appreciation in the exchange rate of the shekel against the dollar of 3.1% in the same quarter last year.

In the first nine months of 2007, the exchange rate of the shekel against the dollar appreciated by 5.0%, compared with appreciation in the exchange rate of the shekel against the dollar of 6.5% in the same period last year.



The Company has liabilities to its employees for severance pay, retirement plans, sick pay, and vacation pay as at September 30, 2007 of \$108 million.

Since most of these liabilities are denominated in shekels, whereas the functional currency of the Company is the dollar, these liabilities must be translated into dollars, which causes differences deriving from changes in the exchange rate of the shekel against the dollar. Exchange rate changes are not one-directional, and cause revenues or expenses in the Company's financial statements accordingly. These revenues or expenses do not impact cash flow or operating costs of the Company in the short run. In order to enable a comparison of the Company's business results over time, these revenues or expenses should be neutralized.

In the quarter ended September 30, 2007, expenses for this element totaling \$4.4 million were recorded, compared with the same period last year, in which expenses totaling \$3.8 million were recorded for this element.

In the first nine months of 2007, expenses for this element were recorded totaling \$5.3 million, compared with the \$7.9 million in such expenses recorded in the same period last year.

Presented below are details of the business results, after neutralizing the effect of the exchange rate on the accrued severance pay element, as described above:

For the three-month period ended September 30:	<u>Before neutralizing effect of changes</u>		<u>After neutralizing effect of changes</u>	
	<u>in exchange rate on Company's provisions</u>		<u>in exchange rate on Company's provisions</u>	
	2007	2006	2007	2006
	(in thousands of dollars)			
Operating expenses	415,379	369,690	413,374	367,266
Gross profit	151,336	77,311	153,341	79,735
Gross margin	26.7%	17.3%	27.1%	17.8%
Selling, general and administrative expenses	87,492	68,789	87,233	68,316
Operating income before financing	63,844	8,522	66,108	11,419
Rate of operating income before financing	11.3%	1.9%	11.7%	2.6%
Other income (expenses), net	(2,445)	(241)	(277)	622
Net income for the period	41,153	1,410	45,585	5,170
Net income rate	7.3%	0.3%	8.0%	1.2%
For the nine-month period ended September 30:	<u>Before neutralizing effect of changes</u>		<u>After neutralizing effect of changes</u>	
	<u>in exchange rate on Company's provisions</u>		<u>in exchange rate on Company's provisions</u>	
	2007	2006	2007	2006
	(in thousands of dollars)			
Operating expenses	1,110,380	1,044,846	1,107,587	1,039,816
Gross profit	297,776	203,904	300,569	208,934
Gross margin	21.1%	16.3%	21.3%	16.7%
Selling, general and administrative expenses	225,330	203,354	224,854	202,372
Operating income before financing	72,446	550	75,715	6,562
Rate of operating income before financing	5.1%	0.0%	5.4%	0.5%
Other income (expenses), net	4,174	(1,518)	6,160	399
Net income (loss) for the period	40,150	(17,980)	45,405	(10,051)
Net income (loss) rate	2.9%	(1.4%)	3.2%	(0.8%)

3.5 Segment reporting

Presented below are geographical segment data on a consolidated basis:

Three-month period ended:					
30.09.2007 (unaudited)	North America	Europe	Central Asia and Far East	Rest of world	Total
	(in millions of dollars)				
Revenues **	204.7	256.7	85.5	11.1	558.0
Operating income ***	27.0	64.6	8.8	4.2	104.6
Operating income as % of segment's revenues	13.2%	25.2%	10.3%	37.9%	18.8%
*30.09.2006 (unaudited)					
Revenues **	162.4	193.0	73.4	10.8	439.6
Operating income ***	9.5	30.6	4.6	3.9	48.5
Operating income as % of segment's revenues	5.8%	15.9%	6.3%	36.1%	11.0%
Nine-month period ended:					
30.09.2007 (unaudited)	North America	Europe	Central Asia and Far East	Rest of world	Total
	(in millions of dollars)				
Revenues **	501.0	611.8	240.5	30.1	1,383.4
Operating income ***	41.9	113.4	18.3	9.2	182.8
Operating income as % of segment's revenues	8.4%	18.5%	7.6%	30.7%	13.2%
*30.09.2006 (unaudited)					
Revenues **	441.2	541.4	216.6	28.5	1,227.7
Operating income ***	15.1	76.5	28.9	8.9	129.4
Operating income as % of segment's revenues	3.4%	14.1%	13.3%	31.1%	10.5%

For year ended:					
* 31.12.2006 (audited)	North America	Europe	Central Asia and Far East	Rest of world	Total
	(in millions of dollars)				
Revenues **	580.4	702.9	313.5	36.6	1,633.4
Operating income ***	14.9	84.1	39.5	8.0	146.6
Operating income as % of segment's revenues	2.6%	12.0%	12.6%	22.8%	9.0%

* Restated – see Note 1.3.1 and Note 1.5 to the interim financial statements.

** Revenues are allocated to geographic segments based on the flight destinations.

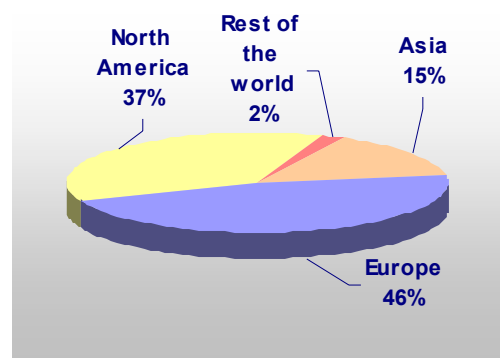
*** Excluding data not allocated to segments, see Note 7 to the interim financial statements.

In the three month period ended September 30, 2007 revenues and operating income percentages increased in all the geographic segments compared with the same period last year.

The increase in the operating income percentages in the third quarter of 2007, compared with the same quarter last year, is due to the increase in the revenue per RPK, and from the improved operating efficiency that is expressed in the increase in passenger load factor.

The improvement that occurred in the North America segment was impacted, in addition to the aforesaid, by the shift to direct flights to Los Angeles and Miami, whereas contributing to the improved operating income percentages in Europe was the discontinuation of flights to Turkey and Cyprus.

**Operating revenues attributed to geographical segments
July-September 2007:**



In the nine-month period ended September 30, 2007, revenues increased in all the geographic segments, compared with the same period last year.

The operating income percentage in the first nine months of 2007 compared with the same period last year, increased in the North America and Europe segments, while they decreased in the Central Asia and Far East segments.

The decrease in the operating income percentage in the Asia and Far East segment is mainly due to the slowdown in the cargo activities in this segment.

4. Seasonal factors

Passenger traffic in Ben-Gurion Airport has a strong seasonal nature. Most of the activity occurs in the summer months, peaking in July-September. The winter months (January-March) are characterized on one hand by low passenger traffic, but on the other hand, the cargo transport of agricultural exports to Europe during those months is higher.

5. Liquidity and financing sources

The cash flows in the three-month period ended September 30, 2007 compared with the same period last year are:

	July-September 2007	July-September *2006	change
	in thousands of dollars	in thousands of dollars	in thousands of dollars
Cash flows from (used for) operating activities	74,083	(4,663)	78,746
Cash flows used for investing activities	(294,422)	(11,799)	(282,623)
Cash flows from (used for) financing activities	150,535	(21,272)	171,807
Net decrease in cash and cash equivalents	(69,804)	(37,734)	(32,070)

* Restated – see Note 1.3.1 and Note 1.5 to the interim financial statements.

In the quarter ended September 30, 2007, the Company had cash from operating activities of \$74.1 million (compared with cash used for operating activities of \$4.7 million in the same period last year), after depositing the proceeds of \$1.9 million from the exercise of options in the funded severance pay provision to cover liabilities of the past.

The change in the Company's cash flows from operating activities in the three-month period ended September 30, 2007, compared with the same period last year, derives mainly from the increase in income in the current period, compared with the income in the same quarter last year and from changes in the trade accounts payable, other payables and trade accounts receivable items.

In the third quarter of 2007, the Company used \$183.8 million for payments on account of the purchase of planes and the purchase of other fixed assets, overhaul of engines, spare parts and accessories (compared with \$33.7 million in the same period last year). In the current period, the Company invested \$110.4 million, net, in short-term deposits (compared with the realization of short-term deposits of \$15.5 million, net, in the same period last year).

In total, the Company used \$294.4 million for investing activities in the three-month period ended September 30, 2007, compared with \$11.8 million used in investing activities in the same quarter last year.

In the three-month period ended September 30, 2007, the Company received proceeds from long-term loans of \$219.4 million to finance the purchase of the two new planes, while it used \$61.3 million to repay long-term loans (compared with \$20.2 million in the same period last year) and to obtain long-term loans totaling \$7.6 million.

In total, in the third quarter of the year, cash flows from financing activities of \$150.5 million were provided to the Company, compared with \$21.3 million used in the same period last year.

In the three month period ended September 30, 2007, the State deposited \$14.2 million in the severance pay fund of the Company's employees pursuant to the terms of the prospectus (compared with \$0.1 million in the same period last year). This activity does not affect the Company's cash flows.

The cash flows in the nine-month period ended September 30, 2007 compared with the same period last year are:

	January- September 2007	January- September *2006	change
	in thousands of dollars	in thousands of dollars	in thousands of dollars
Cash flows from operating activities	178,081	70,107	107,974
Cash flows used for investing activities	(396,535)	(49,243)	(347,292)
Cash flows from (used for) financing activities	161,439	(51,426)	212,865
Net decrease in cash and cash equivalents	(57,015)	(30,562)	(26,453)

* Restated – see Note 1.3.1 and Note 1.5 to the interim financial statements.

In the nine months ended September 30, 2007, the Company was provided with cash from operating activities of \$178.1 million (compared with cash provided from operating activities of \$70.1 million in the same period last year), after depositing the proceeds of \$24.4 million from the exercise of options in the funded severance pay provision to cover liabilities of the past.

The change in the Company's cash flows from operating activities in the first nine months of 2007, compared with the same period last year, derives mainly from the income in the current period, compared with a loss in the same period last year and from changes in the trade accounts payable and other payables items.

In the nine-month period ended September 30, 2007, the Company used \$221.2 million for payments on account of the purchase of planes and the purchase of other fixed assets, overhaul of engines, spare parts and accessories (compared with \$104.8 million in the same period last year). In the current period, the Company invested \$178.9 million, net, in short-term deposits (compared with the realization of short-term deposits of \$49.1 million, net, in the same period last year).

In the nine-month period ended September 30, 2007, the Company used \$396.5 million for investing activities, compared with \$49.2 million in the same period last year.

In the nine-month period ended September 30, 2007, the Company received proceeds from long-term loans of \$219.4 million to finance the purchase of the two new planes, as well as proceeds from the exercise of options of \$31.8 million, while it used \$81.4 million to repay long-term loans (compared with \$49.7 million in the same period last year) and to obtain long-term loans totaling \$7.6 million.

In total, in the first nine months of 2007, cash flows from financing activities of \$161.4 million were provided to the Company, compared with \$51.4 million used in the same period last year.

In the nine month period ended September 30, 2007, the State deposited \$25.3 million in the severance pay fund of the Company's employees pursuant to the terms of the prospectus (compared with \$0.8 million in the same period last year). This activity does not affect the Company's cash flows.

Total cash and cash equivalents and short-term investments as at September 30, 2007 amounted to \$272.7 million, compared with \$150.8 million as at December 31, 2006 (September 30, 2006 - \$126.9 million).

6. Qualitative reporting on exposure to and management of market risks

6.1 Company market risks management policy, officials responsible for their management and means of controlling and executing policy

The Company has a Board of Directors committee for market risks management headed by the chairman of the finance, budget and financial statements committee, Mr. Nadav Palti, who is responsible for prescribing the policy for covering the existing exposure. The CFO is responsible for executing the policy and reporting to the market risks management committee.

The market risks management committee prescribes the framework for future consumption of jet fuel to be covered with financial hedges. Likewise, from time to time, the committee evaluates the need to invest in derivatives to reduce the exposure from interest risks and currency risks.

In the current period, the Company continued to implement the corporation's policies for the management of market risks and means of control, as described in the Report of the Board of Directors on the State of the Corporation's Affairs for the year ended December 31, 2006 and the notes to the financial statements as at such date.

For details on the policy that was actually implemented, see Par. 6.2, 6.3 and 6.4 below.

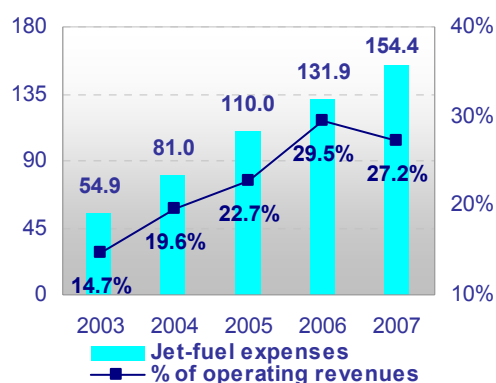
6.2 Hedging jet fuel prices (HJFP)

Presented below are data on positions in transactions hedging jet fuel prices that were executed by the Company (recognized in accounting terms) as at September 30, 2007:

	Type of transaction	Period	Transaction's currency	Fair value in thousand of dollars
HJFP	Financial instruments	Up to One year	US dollar	9,733
HJFP	Financial instruments	Over One year	US dollar	485
Total			US dollar	10,218

For additional information, see Note 20.B.1 of the Periodic Report as at December 31, 2006.

Total Jet-fuel expenses & % of operating revenues, third quarter by years: (in millions US dollars)



6.3 Hedging interest on loans

In the years 2005 and 2006, the Company executed, with banking institutions in Israel, hedges of the exposure in its long-term credit portfolio, due to changes in interest rates.

In the current period, no other transactions were executed. Subsequent to the balance sheet date, the Company executed additional interest hedges, in accordance with the policy prescribed by the Board of Directors committee for management of market risks, as described in the Report of the Board of Directors on the State of the Corporation's Affairs for the year ended December 31, 2006 and the notes to the financial statements as at such date.

Some of these financial instruments are not recognized for accounting purposes as hedge transactions. The fair value of these instruments as at September 30, 2007 is \$2.3 million, which is stated in the financial statements in the line item "receivables and other assets". Additional agreements are recognized for accounting purposes as hedge transactions.

After executing these hedges, as at September 30, 2007, 55% of the balance of the Company's loans is at fixed interest rates. The percentage of the Company's loans at fixed interest has gradually decreased for a period of up to 3 years.

It should be noted that in the first nine months of 2007, in accordance with the instruments chosen to hedge interest exposures, some of the hedging transactions changed according to market interest, after crossing the exit point stipulated in the agreements with the banks as at that date.

For additional information on these transactions, see Note 20.B.2 to the periodic report as at December 31, 2006.

6.4 Exchange rate hedges

During the reported period, the Company executed several financial transactions intended to protect the Company from decreases in the exchange rate of the dollar against the shekel for the year 2008. These transactions are not recognized for accounting purposes. The fair value of these instruments as at September 30, 2007 is \$1.3 million, which is included in the financial statements in "receivables and other assets".

6.5 Sensitivity analysis reporting

During the reported period, no material changes occurred in the market risks that were reported in the Directors Report for the year 2006

7. Disclosure regarding adoption of International Financial Reporting Standards (IFRS)

Within the scope of the Board of Directors Report for the quarter ended June 30, 2007, the expected quantitative effect of the change to International Financial Reporting Standards (IFRS) was presented.

During the quarter ended September 30, 2007, there was no material change or innovation related to preparations for the transition to IFRS Standards and its expected effects on the Company.

8. Linkage basis report

Presented below is the consolidated linkage basis report as at September 30, 2007:

	Denominated in or linked to the dollar	In Israeli currency	Denominated in or linked to the euro	Denominated in or linked to other currencies	Non- monetary items	Total
(in thousands of dollars)						
Assets						
Cash and cash equivalents	82,904	880	623	4,736	-	89,143
Short-term investments	175,000	7,543	1,022	-	-	183,565
Trade accounts receivable	136,544	61	15,316	19,488	-	171,409
Receivables and other current assets	15,679	7,076	-	1,599	34,471	58,825
Deferred income taxes	-	-	-	-	7,831	7,831
Inventory	-	-	-	-	15,095	15,095
Long-term bank deposits	-	2,076	-	-	-	2,076
Investment in another company	1,865	-	-	-	-	1,865
Investees	1,645	-	-	-	695	2,340
Fixed assets	-	-	-	-	1,293,818	1,293,818
Other assets	-	-	-	-	3,626	3,626
	413,637	17,636	16,961	25,823	1,355,536	1,829,593
Liabilities & Equity						
Short-term borrowings	(63,762)	(106)	(1,492)	(91)	-	(65,451)
Trade accounts payable	(115,638)	(28,472)	(25,362)	(13,181)	-	(182,653)
Payables and other current liabilities	(91,614)	(104,933)	(3,693)	(2,297)	(199,570)	(402,107)
Long-term loans from financial institutions	(736,191)	-	-	-	-	(736,191)
Accrued severance pay, net	(24,063)	(34,074)	(6,465)	(4,030)	-	(68,632)
Deferred income taxes	-	-	-	-	(61,369)	(61,369)
Other long-term liabilities	(473)	-	-	-	-	(473)
Shareholders' equity	-	-	-	-	(312,717)	(312,717)
	(1,031,741)	(167,585)	(37,012)	(19,599)	(573,656)	(1,829,593)
Assets, net of liabilities (liabilities net of assets)	(618,104)	(149,949)	(20,051)	6,224	781,880	-

Presented below is the consolidated linkage basis report as at September 30, 2006:

	Denominated in or linked to the dollar	In Israeli currency	Denominated in or linked to the euro	Denominated in or linked to other currencies	Non- monetary items	Total
(in thousands of dollars)						
Assets						
Cash and cash equivalents	55,580	4,282	391	3,114	-	63,367
Short-term investments	63,500	-	-	-	-	63,500
Trade accounts receivable	130,346	90	13,234	16,352	-	160,022
Receivables and other current assets	17,117	4,583	635	1,188	25,630	49,153
Deferred income taxes	-	-	-	-	22,619	22,619
Inventory	-	-	-	-	19,072	19,072
Long-term bank deposits	-	1,800	-	-	-	1,800
Investment in another company	1,905	-	-	-	-	1,905
Investees	1,229	-	-	-	764	1,993
Fixed assets	74,202	-	-	-	1,110,762	1,184,964
Other assets	-	-	-	-	3,249	3,249
	343,879	10,755	14,260	20,654	1,182,096	1,571,644
Liabilities & Equity						
Short-term borrowings	(102,426)	(565)	(190)	(281)	-	(103,462)
Trade accounts payable	(103,199)	(22,822)	(19,090)	(8,388)	-	(153,499)
Payables and other current liabilities	(81,608)	(96,473)	(2,730)	(2,086)	(161,055)	(343,952)
Long-term loans from financial institutions	(547,442)	-	-	-	-	(547,442)
Accrued severance pay, net	(20,082)	(95,277)	(5,588)	(3,918)	-	(124,865)
Deferred income taxes	-	-	-	-	(68,205)	(68,205)
Other long-term liabilities	(869)	-	-	-	-	(869)
Shareholders' equity	-	-	-	-	(229,350)	(229,350)
	(855,626)	(215,137)	(27,598)	(14,673)	(458,610)	(1,571,644)
Assets, net of liabilities (liabilities net of assets)						
	(511,747)	(204,382)	(13,338)	5,981	723,486	-

Presented below is the consolidated linkage basis report as at December 31, 2006:

	Denominated in or linked to the dollar	In Israeli currency	Denominated in or linked to the euro	Denominated in or linked to other currencies	Non- monetary items	Total
(in thousands of dollars)						
Assets						
Cash and cash equivalents	127,167	15,011	530	3,450	-	146,158
Short-term investments	4,000	682	-	-	-	4,682
Trade accounts receivable	102,052	109	11,872	18,511	-	132,544
Receivables and other current assets	13,431	5,227	857	2,867	24,960	47,342
Deferred income taxes	-	-	-	-	30,645	30,645
Inventory	-	-	-	-	17,190	17,190
Long-term bank deposits	-	1,836	-	-	-	1,836
Investment in another company	1,829	-	-	-	-	1,829
Investees	1,228	-	-	-	1,052	2,280
Fixed assets	-	-	-	-	1,176,528	1,176,528
Other assets	-	-	-	-	3,455	3,455
	249,707	22,865	13,259	24,828	1,253,830	1,564,489
Liabilities & Equity						
Short-term borrowings	(104,359)	(126)	(595)	(20)	-	(105,100)
Trade accounts payable	(86,522)	(22,964)	(23,126)	(12,378)	-	(144,990)
Payables and other current liabilities	(88,830)	(96,361)	(2,830)	(2,325)	(142,345)	(332,691)
Long-term loans	(566,104)	-	-	-	-	(566,104)
Accrued severance pay, net	(19,783)	(96,010)	(6,420)	(3,958)	-	(126,171)
Deferred income taxes	-	-	-	-	(74,603)	(74,603)
Other long-term liabilities	(730)	-	-	-	-	(730)
Shareholders' equity	-	-	-	-	(214,100)	(214,100)
	(866,328)	(215,461)	(32,971)	(18,681)	(431,048)	(1,564,489)
Assets, net of liabilities (liabilities net of assets)	(616,621)	(192,596)	(19,712)	6,147	822,782	-

9. Disclosure in the Report of the Board of Directors regarding the financial statement approval process

The body charged with ultimate control in the Company is its board of directors.

At the approval date of these financial statements, the members of the board of directors are: Professor Israel (Izzy) Borovich - Chairman of the Board of Directors, Mrs. Tamar Moses Borovitz - Deputy Chairman, Nadav Palti - Chairman of the Finance, Budget and Financial Statements Committee, Ami Sagis, Shimon Katznelson - director from the public, Yair Rabinovich - director from the public, Amnon Lipkin-Shachak, Eran Ilan.

Within the framework of the board of directors, the Company operates several committees, including the Audit Committee, the Market Risks Management Committee, the Human Resources and Appointments Committee and the Finance, Budget and Financial Statements Committee, which has four members, including an external director. The four members of the committee have accounting and financial expertise, as defined in the Companies Law, 1999, and the regulations promulgated thereunder.

A draft of the financial statements was sent in advance for the review of the members of the board of directors.

The Finance, Budget and Financial Statements Committee meets for extensive and thorough discussion of the draft financial statements, in the presence of the independent auditor. The Chief Executive Officer and the Chief Financial Officer present the members of the committee with extensive details on the financial statements, including detailed financial analyses about the Company's performance during the reporting period.

The committee examines the significant financial reporting issues, including material transactions that are not in the ordinary course of business – if any, the significant assessments and critical estimates that were applied in the financial statements, the reasonableness of the data, the accounting policy applied and the changes that occurred in them, if any, the application of the principle of fair disclosure in the financial statements and various aspects of control and management of risks.

When complex or significant issues are on the agenda, special discussions are held by the Finance, Budget and Financial Statements Committee about the matter on the agenda with the participation of the independent auditor.

The committee holds a discussion about the financial statements presented to it, including directing questions to the members of management present and to the independent auditor. Likewise, the independent auditor is asked to present his comments to the committee members – if any, including accounting policy applied and special events that arose during the audit.

The committee adopts a resolution to recommend to the Company's board of directors to approve the financial statements, subject to making corrections, changes and supplements – if so requested by the members of the committee.

The financial statements are presented to the members of the board in a separate meeting, in which the CEO, the CFO and other officers of the Company participate, also attended by the independent auditor.

A discussion is also held in this forum regarding the financial statements, including questions addressed to the independent auditor and members of the Company's management, and special

issues in the reporting period are presented. At the end of the discussion, the board of directors adopts a resolution on approval of the financial statements.

10. Explanation of matters to which the company's independent auditors draw attention in their review report on the interim financial statements

The Company's independent auditors draw attention, in their review report on the interim financial statements, to the following matters:

- A. To Note 5 to the interim financial statements - regarding legal proceedings against the Company.
- B. To Note 1.5 to the interim financial statements - regarding the restatement of the financial statements as at December 31, 2006 and for the year then ended, and as at September 30, 2006 and for the periods of nine months and three months then ended, due to the first-time adoption of Accounting Standard No. 27 - Fixed Assets, and for the correction of the deferred taxes liability.

Although the matters to which the independent auditors drew attention do not affect the change in the uniform wording of the auditor's report, the drawing of attention is required because of the possible material effect on the Company.

11. Subsequent events

Regarding subsequent events (related to a dividend distribution, a new claim lodged against the Company and a new plan for senior employee options plan), see Note 8 to the interim financial statements.

Prof. Israel (Izzy) Borovich

Chairman of the Board

Haim Romano

Chief Executive Officer

November 20, 2007

El Al Israel Airlines Ltd.

Condensed Consolidated Interim Financial Statements

As at September 30, 2007

(Unaudited)

El Al Israel Airlines Ltd.

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Board of Directors of
El Al Israel Airlines Ltd.
Ben-Gurion Airport

Gentlemen:

**Re: Review of Condensed Unaudited Interim Consolidated Financial Statements
As at September 30, 2007 and for the periods of nine months and three months then ended**

At your request, we reviewed the condensed interim consolidated balance sheet of El Al Israel Airlines Ltd. ("the Company") as at September 30, 2007 and the consolidated statements of operations, the statements of changes in shareholders' equity and the consolidated interim statements of cash flows for the periods of nine months and three months then ended.

Our review was performed in accordance with the procedures prescribed by the Institute of Certified Public Accountants in Israel. The procedures included, inter alia: reading the aforementioned financial statements, reading the minutes of meetings of shareholders and meetings of the board of directors and its committees, and making inquiries with persons responsible for the financial and accounting matters.

We were provided with the reports of other auditors regarding the review of the condensed interim financial statements of subsidiaries, the assets of which constitute approximately 0.8% of the total assets included in the condensed interim consolidated balance sheet, and their revenues from operations constitute 0.4% and 0.3% of total revenues included in the condensed consolidated statements of operations for the periods of nine months and three months ended September 30, 2007.

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

In performing our review, including reading of the reports of other auditors, nothing came to our attention that indicates that any material modifications should be made in the aforementioned interim financial statements, so that they would conform with generally accepted accounting principles, and with Chapter IV of the Israeli Securities Regulations (Periodic and Immediate Reports), 1970.

We draw your attention to the following matters:

- A. To Note 5 regarding legal proceedings against the Company.
- B. To Note 1.5 regarding the restatement of the financial statements as at December 31, 2006 and for the year then ended, and as at September 30, 2006 and for the periods of nine months and three months then ended, due to the first-time application of Accounting Standard No. 27 – Fixed Assets, and for the correction of the deferred tax liability.

Respectfully,

Brightman Almagor
Certified Public Accountants

Tel-Aviv, November 20, 2007

Audit • Tax • Consulting • Financial Advisory.

A member firm of
Deloitte Touche Tohmatsu

El Al Israel Airlines Ltd.

Condensed Consolidated Interim Balance Sheets

	<u>As at September 30</u>		<u>As at</u> <u>December 31</u>
	<u>2 0 0 7</u>	<u>2 0 0 6</u>	<u>2 0 0 6</u>
	<u>Unaudited</u>		<u>Audited</u>
	<u>(in thousand US dollars)</u>		
<u>Current assets</u>			
Cash and cash equivalents	89,143	63,367	146,158
Short-term investments	183,565	63,500	4,682
Trade accounts receivable	171,409	160,022	132,544
Receivables and other current assets	58,825	49,153	47,342
Deferred taxes	7,831	22,619	30,645
Inventory	15,095	19,072	17,190
	<u>525,868</u>	<u>377,733</u>	<u>378,561</u>
<u>Investments</u>			
Long-term bank deposits	2,076	1,800	1,836
Investment in another company	1,865	1,905	1,829
Investees	2,340	1,993	2,280
	<u>6,281</u>	<u>5,698</u>	<u>5,945</u>
<u>Fixed assets</u>	<u>1,293,818</u>	<u>(*) 1,184,964</u>	<u>(*) 1,176,528</u>
<u>Other assets</u>	<u>3,626</u>	<u>3,249</u>	<u>3,455</u>
	<u>1,829,593</u>	<u>1,571,644</u>	<u>1,564,489</u>

(*) Restated - see Note 1.5.

El Al Israel Airlines Ltd.

Condensed Consolidated Interim Balance Sheets

	As at September 30		As at
	2007	2006	December 31
	Unaudited		Audited
	(in thousand US dollars)		
<u>Current liabilities</u>			
Short-term borrowings and current maturities	65,451	103,462	105,100
Trade accounts payable	182,653	153,499	144,990
Payables and other current liabilities	402,107	343,952	332,691
	<u>650,211</u>	<u>600,913</u>	<u>582,781</u>
<u>Long-term liabilities</u>			
Long-term loans from financial institutions	736,191	547,442	566,104
Accrued severance pay, net	68,632	124,865	126,171
Deferred income taxes	61,369	(*) 68,205	(*) 74,603
Other long-term liabilities	473	869	730
	<u>866,665</u>	<u>741,381</u>	<u>767,608</u>
Total liabilities	<u>1,516,876</u>	<u>1,342,294</u>	<u>1,350,389</u>
<u>Shareholders' equity</u>			
Share capital	155,012	131,536	131,536
Premium on shares	9,248	904	904
Capital reserve from transactions with a former controlling party	243,787	(*) 218,498	(*) 218,498
Capital reserve from an employee options program	3,940	1,900	2,582
Accumulated deficit	(99,270)	(*) (123,488)	(*) (139,420)
	<u>312,717</u>	<u>229,350</u>	<u>214,100</u>
	<u>1,829,593</u>	<u>1,571,644</u>	<u>1,564,489</u>

(*) Restated - see Note 1.5.

Prof. Israel (Izzy) Borovich
Chairman of the Board

Haim Romano
Chief Executive
Officer

Nissim Malki
Chief Financial Officer

Approval date of the financial statements - Ben-Gurion Airport, November 20, 2007.

The accompanying notes are an integral part of the condensed interim financial statements

El Al Israel Airlines Ltd.
Condensed Consolidated Interim Statement of Operations

	Nine-month period ended September 30		Three-month period ended September 30		Year ended December 31
	2 0 0 7	2 0 0 6	2 0 0 7	2 0 0 6	2 0 0 6
	Unaudited		Unaudited		Audited
	(in thousand US dollars)				
Operating revenues	1,408,156	1,248,750	566,715	447,001	1,665,446
Operating expenses	1,110,380	(*) 1,044,846	415,379	(*) 369,690	(*) 1,394,159
Gross profit	297,776	203,904	151,336	77,311	271,287
Selling expenses	159,365	135,714	65,904	46,673	187,805
General and administrative expenses	65,965	67,640	21,588	22,116	91,952
	225,330	203,354	87,492	68,789	279,757
Operating income (loss) before net financing expenses	72,446	550	63,844	8,522	(8,470)
Net financing expenses	27,035	21,860	10,386	6,725	29,492
Operating income (loss) after net financing expenses	45,411	(21,310)	53,458	1,797	(37,962)
Other income (expenses), net	4,174	(*) (1,518)	(2,445)	(*) (241)	(*) (2,764)
Pre-tax income (loss)	49,585	(22,828)	51,013	1,556	(40,726)
Income tax savings (expenses)	(9,580)	(*) 4,719	(9,914)	(*) (180)	(*) 6,397
Income (loss) after income taxes	40,005	(18,109)	41,099	1,376	(34,329)
Company's equity in earnings of affiliates, net	145	129	54	34	417
Net income (loss) for the period	40,150	(*) (17,980)	41,153	(*) 1,410	(*) (33,912)
Basic earnings (loss) per share (NIS 1 par value) – in dollars	0.09	(*) (0.04)	0.08	0.004	(*) (0.08)
Number of shares used in the computation of basic EPS (in thousands)	444,298	400,643	495,719	400,788	400,680
Fully diluted earnings (loss) per share (NIS 1 par value) – in dollars	0.08	(*) (0.04)	0.08	(*) 0.003	(*) (0.08)
Number of shares used in the computation of fully diluted EPS (in thousands)	495,721	400,643	495,719	495,721	400,680

(*) Restated – see Note 1.5.

The accompanying notes are an integral part of the condensed interim financial statements

El Al Israel Airlines Ltd.

Condensed Interim Statements of Changes in Shareholders' Equity

	<u>Share capital</u>	<u>Premium on shares</u>	<u>Capital reserve</u>		<u>Accumulated deficit</u>	<u>Dividend declared</u>	<u>Total</u>
			(**)	(***)			
	(in thousand US dollars)						
Nine-month period ended							
September 30, 2007							
(unaudited):							
Balance – January 1, 2007	131,536	904	(*) 218,498	2,582	(*) (139,420)	-	(*) 214,100
Receipts on account of Government of Israel debt	-	-	25,289	-	-	-	25,289
Exercise of options into shares	23,476	8,344	-	-	-	-	31,820
Benefit value of employee options program	-	-	-	1,358	-	-	1,358
Dividend declared subsequent to balance sheet date (see Note 8)	-	-	-	-	(9,265)	9,265	-
Net income for the period	-	-	-	-	40,150	-	40,150
Balance – September 30, 2007	<u>155,012</u>	<u>9,248</u>	<u>243,787</u>	<u>3,940</u>	<u>(108,535)</u>	<u>9,265</u>	<u>312,717</u>
Three-month period ended							
September 30, 2007							
(unaudited):							
Balance – July 1, 2007	155,012	9,248	229,560	3,513	(140,423)	-	256,910
Receipts on account of Government of Israel debt	-	-	14,227	-	-	-	14,227
Benefit value of employee options program	-	-	-	427	-	-	427
Dividend declared subsequent to balance sheet date (see Note 8)	-	-	-	-	(9,265)	9,265	-
Net income for the period	-	-	-	-	41,153	-	41,153
Balance – September 30, 2007	<u>155,012</u>	<u>9,248</u>	<u>243,787</u>	<u>3,940</u>	<u>(108,535)</u>	<u>9,265</u>	<u>312,717</u>

(*) Restated - see Note 1.5.

(**) From transactions with the former controlling party.

(**) From the employee options plan.

The accompanying notes are an integral part of the condensed interim financial statements

El Al Israel Airlines Ltd.

Condensed Interim Statements of Changes in Shareholders' Equity

	<u>Share capital</u>	<u>Premium on shares</u>	<u>Capital reserve</u> (**) (***) (in thousand US dollars)		<u>Accumulated deficit</u>	<u>Total</u>
Nine-month period ended September 30, 2006 (unaudited):						
Balance – January 1, 2006	131,318	826	(*) 217,723	-	(*) (105,508)	(*) 244,359
Receipts on account of Government of Israel debt	-	-	775	-	-	775
Exercise of options into shares	218	78	-	-	-	296
Benefit value of employee options program	-	-	-	1,900	-	1,900
Loss for the period	-	-	-	-	(*) (17,980)	(*) (17,980)
Balance – September 30, 2006	<u>131,536</u>	<u>904</u>	<u>(*) 218,498</u>	<u>1,900</u>	<u>(*) (123,488)</u>	<u>(*) 229,350</u>
Three-month period ended September 30, 2006 (unaudited):						
Balance – July 1, 2006	131,536	904	(*) 218,425	973	(*) (124,898)	(*) 226,940
Receipts on account of Government of Israel debt	-	-	73	-	-	73
Benefit value of employee options program	-	-	-	927	-	927
Net income for the period	-	-	-	-	(*) 1,410	(*) 1,410
Balance – September 30, 2006	<u>131,536</u>	<u>904</u>	<u>(*) 218,498</u>	<u>1,900</u>	<u>(*) (123,488)</u>	<u>(*) 229,350</u>
Year ended December 31, 2006 (audited):						
Balance – January 1, 2006	131,318	826	(*) 217,723	-	(*) (105,508)	(*) 244,359
Receipts on account of Government of Israel debt	-	-	775	-	-	775
Exercise of options into shares	218	78	-	-	-	296
Benefit value of employee options program	-	-	-	2,582	-	2,582
Loss for the year	-	-	-	-	(*) (33,912)	(*) (33,912)
Balance – December 31, 2006	<u>131,536</u>	<u>904</u>	<u>(*) 218,498</u>	<u>2,582</u>	<u>(*) (139,420)</u>	<u>(*) 214,100</u>

(*) Restated - see Note 1.5.

(**) From transactions with the former controlling party.

(**) From the employee options plan.

The accompanying notes are an integral part of the condensed interim financial statements

El Al Israel Airlines Ltd.**Condensed Consolidated Interim Statements of Cash Flows**

	Nine-month period ended September 30		Three-month period ended September 30		Year ended December 31
	2007	2006	2007	2006	2006
	Unaudited		Unaudited		Audited
	(in thousand US dollars)				
Cash flows – operating activities					
Net income (loss) for the period	40,150	(*)17,980	41,153	(*)1,410	(*) (33,912)
Adjustments required to present net cash flows provided by (used for) operating activities (Appendix A)	162,307	(*) 88,383	34,794	(*)6,063	(*) 132,344
Net cash provided by (used for) operating activities, before deposit of proceeds from exercise of options in funded severance pay, to cover liabilities of the past	202,457	(*) 70,403	75,947	(*)4,653	(*) 98,432
Deposit of proceeds from exercise of options in funded severance pay, to cover liabilities of the past	(24,376)	(296)	(1,864)	(10)	(296)
Net cash provided by (used for) operating activities	178,081	(*)70,107	74,083	(*)4,663	(*) 98,136
Cash flows – investing activities					
Investment in other assets	(446)	(901)	(358)	-	(1,188)
Additions to fixed assets (including general engine overhauls and payments on account of aircrafts)	(221,245)	(*)104,786	(183,761)	(*)33,712	(*) (128,894)
Refund of investment in fixed assets	3,843	-	-	-	-
Proceeds from disposition of fixed assets	360	6,690	163	6,302	6,965
Increase (decrease) in short-term deposits, net	(178,883)	49,094	(110,437)	15,500	107,912
Investments in long-term deposits	(285)	(151)	(79)	(50)	(226)
Realization of long-term deposits	157	489	28	121	560
Investment in supplier deposits	(70)	(46)	(12)	-	(82)
Redemption of supplier deposits	34	41	34	40	73
Decrease in investments and loans to investees, net	-	327	-	-	326
Net cash used for investing activities	(396,535)	(*)49,243	(294,422)	(*)11,799	(*) (14,554)
Cash flows – financing activities					
Proceeds from exercise of options into shares	31,820	296	-	-	296
Receipt of long-term loans from financial institutions	219,420	-	219,420	-	40,000
Repayment of long-term loans from financial institutions	(79,540)	(48,110)	(60,694)	(19,635)	(67,745)
Receipt of other long-term loans	-	488	-	488	1,014
Repayment of other long-term loan	(1,861)	(1,599)	(627)	(564)	(2,248)
Payment on account of costs of obtaining loans	(7,570)	-	(7,570)	-	(1,080)
Increase (decrease) in short-term borrowings, net	(830)	(2,501)	6	(1,561)	(1,590)
Net cash provided by (used for) financing activities	161,439	(51,426)	150,535	(21,272)	(31,353)
Increase (decrease) in cash and cash equivalents	(57,015)	(30,562)	(69,804)	(37,734)	52,229
Cash and cash equivalents at beginning of period	146,158	93,929	158,947	101,101	93,929
Cash and cash equivalents at end of period	89,143	63,367	89,143	63,367	146,158

(*) Restated – see Note 1.5.

The accompanying notes are an integral part of the condensed interim financial statements

El Al Israel Airlines Ltd.
Condensed Consolidated Interim Statements of Cash Flows

Nine-month period ended September 30		Three-month period ended September 30		Year ended December 31
2007	2006	2007	2006	2006
Unaudited		Unaudited		Audited

(in thousand US dollars)

Appendix A – Adjustment required to present net cash flows provided by operating activities:

**Income and expenses not
involving cash flows:**

Depreciation and amortization (including disposal of accessories, components no longer in use and consumption of supplies)	100,693	(*)103,177	34,529	(*)35,952	(*) 134,150
Adjustment in the value of long-term deposits	(112)	(119)	(130)	(56)	(151)
Equity in earnings of affiliates, net of dividends received, net	(60)	(129)	31	(34)	(417)
Increase (decrease) in accrued severance pay, net	(6,884)	9,342	(3,892)	5,715	5,633
Increase in capital reserve from employee options plan	1,358	1,900	427	927	2,582
Capital gains (losses) from disposition of fixed assets, net	1,514	(*)1,522	(49)	(*)1,404	(*)1,642
Adjustment in value of supplier deposits	-	(22)	-	-	58
Deferred tax expenses (savings)	9,580	(*) (4,883)	9,944	(*) 97	(*) (6,510)

Changes in assets and liabilities:

Decrease (increase) in trade accounts receivable	(38,865)	(36,176)	18,138	4,839	(5,844)
Decrease (increase) in receivables and other current assets	(13,088)	(469)	2,454	4,656	93
Decrease in inventory	2,095	3,373	4,236	1,044	5,255
Increase (decrease) in trade accounts payable	37,663	(1,547)	21,405	6,314	(10,056)
Increase (decrease) in payables and other current liabilities	68,426	15,472	(52,291)	(64,102)	9,228
Decrease in other long-term liabilities	(13)	(14)	(8)	(11)	(35)
	<u>162,307</u>	<u>(*)88,383</u>	<u>34,794</u>	<u>(*)6,063</u>	<u>(*) 132,344</u>

Appendix B – Non-cash transactions:

Government of Israel deposits to the employees' severance-pay fund	<u>25,289</u>	<u>775</u>	<u>14,227</u>	<u>73</u>	<u>775</u>
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(*) Restated – see Note 1.5.

The accompanying notes are an integral part of the condensed interim financial statements

El Al Israel Airlines Ltd.
Notes to the Condensed Consolidated Interim Financial Statements
As at September 30, 2007
(Unaudited)

Note 1 – Reporting principles and accounting policies

1.1 The financial statements for the interim periods were prepared in a condensed format, in accordance with generally accepted accounting principles for the preparation of interim financial statements, as prescribed in Standard 14 of the Israel Accounting Standards Board and Chapter IV of the Israeli Securities Regulations (Periodic and Immediate Reports), 1970.

The significant accounting policies adopted in the Company's audited financial statements for the year ended December 31, 2006 were applied on a consistent basis in the report period, except as provided in Notes 1.3.1 and 1.5 below.

These financial statements are to be reviewed in conjunction with the annual financial statements and related notes as at December 31, 2006.

1.2 Presented below are data on the Consumer Price Index (CPI) and exchange rates of the New Israel Shekel (NIS) and Euro relative to the U.S. dollar:

	Consumer Price Index in points	Dollar rate in NIS	Dollar rate in Euro
	<hr/>	<hr/>	<hr/>
As at September 30, 2007	189.10	4.013	0.705
As at September 30, 2006	186.48	4.302	0.789
As at December 31, 2006	184.87	4.225	0.759
Percentage of change –	<hr/> % <hr/>	<hr/> % <hr/>	<hr/> % <hr/>
For the nine-month period ended			
September 30, 2007	2.3	(5.0)	(7.1)
September 30, 2006	0.8	(6.5)	(6.6)
For the three-month period ended			
September 30, 2007	1.3	(5.6)	(5.2)
September 30, 2006	(0.8)	(3.1)	0.3
For the year ended December 31, 2006	(0.1)	(8.2)	(10.2)

El Al Israel Airlines Ltd.

Notes to the Condensed Consolidated Interim Financial Statements

Note 1 – Reporting principles and accounting policies (continued)

1.3 First-time application of new Accounting Standards –

1.3.1 Accounting Standard No. 27 – Fixed Assets

Since January 1, 2007, the Company applies Accounting Standard No. 27 – Fixed Assets" ("the Standard"), which provides the accounting treatment for fixed assets including recognition of assets, determination of their book value and depreciation expenses, and the recognition of related impairment losses. The Standard also provides the required financial statement disclosure about the entity's fixed assets. The Standard provides, inter alia:

The fixed asset item will be measured on the initial recognition date at cost, which includes, in addition to the purchase price of the asset, all of the costs that can be directly attributed to bringing the item to the location and position necessary for it to operate as management intended.

After the initial recognition, the Standard allows an entity to choose between the cost method and the revaluation method as the accounting policy, provided that it is applied consistently for every fixed asset item in the same category.

In the cost method, a fixed asset item will be stated at cost net of accumulated depreciation, and net of accrued impairment losses.

In the revaluation method, a fixed asset item for which its fair value can be reliably measured, will be stated at a revalued amount, which is the fair value on the revaluation date, net of depreciation that accumulated subsequently and net of impairment losses. The revaluations will be performed in a sufficiently orderly manner, in order to verify that the book value is not materially different than the fair value determined on the balance sheet date. If a fixed asset item is revalued, the entire category of fixed assets to which the asset belongs is to be revalued. If the book value of the asset increases as a result of the revaluation, the increase is charged directly to shareholders' equity, in a reserve for revaluation. However, the increase will be recognized in the statement of operations, up to the amount by which the revaluation reverses an impairment loss that was recognized previously in the statement of operations. If the book value of the asset decreases as a result of the revaluation, the decrease will be recognized in the statement of operations. However, the decrease will be charged directly to shareholders' equity, in the reserve for revaluation, up to the amount of any existing credit balance in the reserve for revaluation for that asset.

Every part of fixed assets having a different economic life is to be written-down separately, if its cost is significant relative to the total cost of the item.

The general overhaul costs of an aircraft engine will be capitalized to the balance sheet and will be depreciated over the period of economic benefit deriving from this overhaul. The accounting policy practiced until the Standard took effect is to record the overhaul cost as an expense when the overhaul is performed.

The expected useful life of an asset and the residual value prescribed for the asset will be reviewed at least at the end of every fiscal year, and if a significant change occurs in the expectations for the future economic benefit inherent in the asset, the useful life and/or residual value is to be changed, in order to reflect these changes. Such a change will be treated as a change in accounting estimate and/or the residual value, in order to reflect these changes. Such a change will be treated as a change in accounting estimate.

El Al Israel Airlines Ltd.

Notes to the Condensed Consolidated Interim Financial Statements

Note 1 – Reporting principles and accounting policies (continued)

1.3 First-time application of new Accounting Standards (continued) –

1.3.1 Accounting Standard No. 27 – Fixed Assets (continued)

According to the Standard's provisions, this Standard applies to financial statements related to periods commencing on or after January 1, 2007, and will be applied retroactively, except for an entity that on January 1, 2007 elects the revaluation method as its accounting policy for a category of fixed assets. The difference between the revalued book value of the asset on that date and its cost will constitute the reserve for revaluation on that date.

In April 2007, the Israel Accounting Standards Board published Accounting Standard No. 28 – Amended Transitional Provisions in Accounting Standard No. 27, Fixed Assets ("Standard 28").

For the purpose of the transition to application of Standard 27, Standard 28 allows an entity that intends to adopt the exception provided in International Financial Reporting Standard No. 1 regarding fixed assets in financial statements for periods commencing on January 1, 2008, to apply the Standard on January 1, 2007.

According to this exception, an entity is allowed to present fixed asset items on the transition date at their fair value as an alternative to their cost ("deemed cost").

Likewise, it was provided that an entity that elects fair value as its deemed cost will not restate comparative figures, but will provide disclosure of this fact and of the fair value of every item so treated as of January 1, 2007.

The Company's management decided to apply the measurement of fixed assets by the cost method.

As a result of the application of the Standard's provisions, the Company wrote-down, through a retroactive adjustment, those fixed asset elements that are significant relative to the overall cost of fixed assets, and which have a different economic life.

Regarding the effect of the retroactive adjustment of the financial statements as at December 31, 2006 and as at September 30, 2006 as a result of application of the Standard – see Note 1.5 below.

1.3.2 Accounting Standard No. 26 – Inventory

Commencing January 1, 2007, the Company applies Accounting Standard No. 26, "Inventory" ("the Standard"), which provides the accounting treatment for inventory.

The Standard provides, inter alia, that the inventory will be measured at the lower of cost or its net usage value. The inventory cost will be determined by the first in – first out method (FIFO) or by the weighted average of cost, while consistently using the cost formula for all the inventory having similar nature and usage. In certain cases, the Standard requires that the inventory cost be determined by the specific identification of its costs. The inventory cost includes all of the purchase costs, production costs and other costs incurred in bringing the inventory to its current location and condition.

El Al Israel Airlines Ltd.

Notes to the Condensed Consolidated Interim Financial Statements

Note 1 – Reporting principles and accounting policies (continued)

1.3 First-time application of new Accounting Standards (continued) –

1.3.2 Accounting Standard No. 26 – Inventory (continued)

In cases in which inventory is bought at credit terms, when the arrangement includes a financing element, the inventory will be stated at cost, which agrees with the purchase cost in cash, and the financing element will be recognized as a financing expense over the credit period.

The amount of any decline in value of inventory to its net usage value, and any inventory losses are recognized in income and loss in the period they occurred. The amount of the reversal of any decline in value of inventory deriving from an increase in the net realization value is recognized in income and loss in the period in which the reversal occurred.

Pursuant to the Standard's provisions, this Standard was applied retroactively.

The Standard did not have an effect on the Company's financial position, operating results and cash flows.

1.3.3 Accounting Standard No. 23 – Accounting Treatment of Transactions between an Entity and its Controlling Owner

In December 2006, the Israel Accounting Standards Board published Accounting Standard No. 23, Accounting Treatment of Transactions between an Entity and its Controlling Owner ("the Standard"). The Standard binds entities that are subject to the Israeli Securities Law, 1968.

The Standard provides the accounting treatment for accounting transactions between an entity and its controlling owner that involve the transfer of an asset, assumption of liabilities, indemnification and waiver, and loans. The Standard does not apply to a business combination under common control.

The Standard provides that the valuation basis of transactions between an entity and its controlling shareholder is fair value; transactions having the nature of an owners' investment or distribution to owners belong in shareholders' equity and are not to be included in the operating results of the controlled body; differences between the proceeds determined in transactions between an entity and its controlling owner and between the fair value of those transactions, will be charged to shareholders' equity. Current and deferred taxes charged to shareholders' equity for transactions with controlling owners will also be charged directly to shareholders' equity.

The Standard applies to transactions between an entity and its controlling owner, executed after January 1, 2007 and to a loan given or received from a controlling owner before the effective date of the Standard, which is in effect from the date of the Standard.

The Standard did not have an effect on the Company's financial position, operating results and cash flows.

El Al Israel Airlines Ltd.

Notes to the Condensed Consolidated Interim Financial Statements

Note 1 – Reporting principles and accounting policies (continued)

1.3 First-time application of new Accounting Standards (continued) –

1.3.4 Accounting Standard No. 30 – Intangible Assets

Commencing January 1, 2007, the Company applies Accounting Standard No. 30, "Intangible Assets" ("the Standard"), which provides the accounting treatment for intangible assets that are not covered in another Standard, and also provides the financial statement disclosure requirements for intangible assets.

An intangible asset qualified for recognition as an asset will initially be measured at cost.

After initial recognition, the Standard permits the entity to elect measurement as follows:

- (a) By the cost model. According to this model, an intangible asset will be stated at cost net of accumulated amortization and net of accrued impairment losses; or
- (b) Regarding intangible assets that have an active market, presentation is at revalued amounts based on their fair value on the revaluation date, net of amortization accumulated subsequently, and net of impairment losses that accrued subsequently. The revaluation amount is charged directly to shareholders' equity, in reserve for revaluation.

An entity is to assess whether the useful life of the intangible asset is specified or unspecified. An intangible asset with a specified useful life will be amortized over its useful life, subject to an impairment evaluation. An intangible asset having an unspecified useful life is not amortized. Instead, an evaluation of decline in value is to be performed once a year, or more frequently if there are signs indicating that the asset may have sustained a decline in value.

The Standard applies to financial statements commencing on or after January 1, 2007, and is applied retroactively, except for certain exceptions provided in the Standard.

The Standard did not have an effect on the Company's financial statements.

1.4 Effect of new Accounting Standards in the period prior to their application

Accounting Standard No. 29 – Adoption of International Financial Reporting Standards (IFRS)

In July 2006, the Israel Accounting Standards Board published Accounting Standard No. 29, "Adoption of International Financial Reporting Standards (IFRS)" ("the Standard" or "Standard 29").

The Standard provides that the financial statements of entities that are subject to the Israeli Securities Law and obligated to report according to the regulations of this law, except for foreign corporations, as defined in the Securities Law, will be prepared as from reporting periods commencing January 1, 2008 in accordance with the International Financial Reporting Standards (IFRS) and their interpretations, which are published by the International Accounting Standards Board (IASB).

El Al Israel Airlines Ltd.

Notes to the Condensed Consolidated Interim Financial Statements

Note 1 – Reporting principles and accounting policies (continued)

1.4 Effect of new Accounting Standards in the period prior to their application (continued)

An entity that will apply the IFRS Standards as from January 1, 2008, and will choose to report comparative figures for the year 2007 alone, in accordance with the IFRS Standards, will be required to prepare an opening balance sheet as at January 1, 2007 in accordance with the IFRS Standards ("opening balance sheet").

The transition to reporting in accordance with IFRS Standards will be carried out in accordance with IFRS Standard 1, initial adoption of IFRS Standards. IFRS Standard 1 provides rules on how an entity will carry out the transition from the previous financial reporting on the basis of previous local accounting principles to financial reporting based on the IFRS. IFRS Standard 1 supercedes all transitional provisions provided in the other IFRS Standards (including transitional provisions provided in previous local accounting standards) and provides that all the international financial reporting standards are to be adopted retroactively in the opening balance sheet. However, IFRS 1 grants accommodations for certain matters by not imposing the obligation to apply them retroactively. Additionally, IFRS 1 provides several exceptions regarding the retroactive application of certain aspects of other IFRS Standards.

1.5 Restatement -

The financial statements as at December 31, 2006 and for the year then ended and as at September 30, 2006, and for the periods of nine months and three months then ended, were retroactively adjusted, in accordance with Accounting Standard No. 27 – Fixed Assets ("the Standard"), as discussed in Note 1.3.1.

Presented below are the changes made as a result of the Standard's taking effect:

1. The cost of general overhaul of engines was separated from the original cost of the aircraft and depreciated based on the period of economic benefit from the overhaul (an average of 8 years).
2. The cost of subsequent overhaul is capitalized in fixed assets and is depreciated, as aforesaid, compared with the accounting policy practiced until the Standard took effect, whereby the overhaul was charged to operating expenses.
3. A capital gain recorded in the third quarter of 2006 on the sale of a cargo plane was retroactively adjusted, as a result of the change in the net book value of that plane on the date of sale.
4. An increase in fixed assets as at December 31, 2006 and June 30, 2006, which required an accrual of deferred taxes payable of \$7,147 thousand and \$6,976 thousand, respectively.

Likewise, within the scope of processing fixed assets data, it was found that the depreciation differences that were taken into account in the past for calculating the deferred tax liability must be changed. This change increases the deferred tax liability as at December 31, 2006 and September 30, 2006 by additional amounts of \$37,188 thousand and \$38,955 thousand, respectively.

El Al Israel Airlines Ltd.**Notes to the Condensed Consolidated Interim Financial Statements****Note 1 – Reporting principles and accounting policies (continued)****1.5 Restatement (continued) -**

The effects on the financial statements of the restatement for the above matters are as follows:

A. Balance sheets

	As at September 30, 2006			As at December 31, 2006		
	Before restatement	Effect of restatement	As reported in these financial statements	Before restatement	Effect of restatement	As reported in these financial statements
	(Unaudited)			(Audited)		
Fixed assets	1,157,927	27,037	1,184,964	1,148,389	28,139	1,176,528
Deferred taxes payable	(22,274)	(45,931)	(68,205)	(30,268)	(44,335)	(74,603)
Capital reserve from transactions with former controlling owner	(299,894)	81,396	(218,498)	(299,894)	81,396	(218,498)
Accumulated deficit	185,990	(62,502)	123,488	204,620	(65,200)	139,420
Total shareholders' equity	(248,244)	18,894	(229,350)	(230,296)	16,196	(214,100)

B. Statements of operations:

	For the period of nine months ended September 30, 2006			For the period of three months ended September 30, 2006			For the year ended December 31, 2006		
	Before restatement	Effect of restatement	As reported in these financial statements	Before restatement	Effect of restatement	As reported in these financial statements	Before restatement	Effect of restatement	As reported in these financial statements
	(Unaudited)			(Unaudited)			(Audited)		
Operating expenses	1,052,236	(7,390)	1,044,846	373,919	(4,229)	369,690	1,402,652	(8,493)	1,394,159
Other expenses (income), net	(3,052)	4,570	1,518	(4,329)	4,570	241	(1,806)	4,570	2,764
Tax (savings) expenses, net	217	(4,936)	(4,719)	166	14	180	134	(6,531)	(6,397)
Loss (Net income) for the period	25,736	(7,756)	17,980	(1,765)	355	(1,410)	44,366	(10,454)	33,912
Basic (earnings) loss per share in dollars	0.06	(0.02)	0.04	(0.004)	-	(0.004)	0.11	(0.03)	0.08
Fully-diluted (earnings) loss per share in dollars	0.06	(0.02)	0.04	(0.004)	0.001	(0.003)	0.11	(0.03)	0.08

El Al Israel Airlines Ltd.**Notes to the Condensed Consolidated Interim Financial Statements****Note 1 – Reporting principles and accounting policies (continued)****1.5 Restatement (continued) -**

C. Statement of cash flows:

	For the period of nine months ended September 30, 2006			For the period of three months ended September 30, 2006			For the year ended December 31, 2006		
	Before restatement (in thousand US dollars)	Effect of restatement	As reported in these financial statements	Before restatement (in thousand US dollars)	Effect of restatement	As reported in these financial statements	Before restatement (in thousand US dollars)	Effect of restatement	As reported in these financial statements
			(Unaudited)			(Unaudited)			(Audited)
Cash flows provided by (used for) operating activities	49,107	21,000	70,107	(14,363)	9,700	(4,663)	73,436	24,700	98,136
Cash flows provided by (used for) investing activities	(28,243)	(21,000)	(49,243)	(2,099)	(9,700)	(11,799)	10,146	(24,700)	(14,554)

Note 2 – Seasonal factors

Passenger traffic in Ben-Gurion Airport is characterized as strongly impacted by seasonal factors. Most of the activity is in the summer months, peaking in the months of July-September. The winter months (January-March) are characterized by lower passenger travel activity.

Note 3 – Fixed assets

In July and August 2007, the Company received two new 777-200 model aircraft purchased by the Company from Boeing.

In July 2007, a financing agreement was signed with a consortium of foreign banking corporations for the purpose of purchasing the aforementioned planes. At the same time, the EXIM Bank furnished a guarantee to secure this financing.

For the first aircraft delivered to the Company in July 2007, the Company received a loan of \$109 million, of which \$88 million is earmarked for payment of the balance of the aircraft's price to Boeing, as well as the costs related to raising the financing. The balance of \$21 million for the part of the independent financing furnished by the Company for the purchase of the aircraft was returned to the Company.

For the second aircraft, which was delivered to the Company in August 2007, the Company received a loan of \$110 million, of which \$88 million is earmarked for payment of the balance of the aircraft's price to Boeing, as well as the costs related to raising the financing. The balance of \$22 million for the part of the independent financing furnished by the Company for the purchase of the aircraft was returned to the Company.

The loan to finance the purchase of the two aircrafts, and the related expenses, are for a period of 12 years and include a "balloon" principal payment to be made at the end of the period. The loan is at variable interest of Libor + a margin, to be repaid in quarterly installments. The aircrafts are pledged through a trust to EXIM, which, as noted, furnished a guarantee in favor of the financing banks.

El Al Israel Airlines Ltd.

Notes to the Condensed Consolidated Interim Financial Statements

Note 4 – Share capital and premium

Options (Series 1) that were issued by the Company and call options (Series B) that were issued by the State of Israel were exercisable until June 5, 2007.

In the period from January 1, 2007 through June 5, 2007, the public exercised 94,930,801 options (Series 1) to the same number of ordinary shares, NIS 1 par value each, issued by the Company, in consideration for \$31,820 thousand.

The proceeds received by the Company from the exercise of the options (Series 1) as noted, were deposited in the severance pay fund of eligible employees, except for NIS 28 million not yet deposited, which are included in short-term deposits as of September 30, 2007.

The Company is examining for the existence of limitations on the use of the balance of the proceeds, as noted, pursuant to its agreement with the State and employee representatives that was signed on the eve of the privatization.

Likewise, during the nine-month and three-month periods ended September 30, 2007, the State deposited \$25,289 thousand and \$14,227 thousand in the severance pay fund of eligible employees, respectively, originating in the exercise of options (Series B) by the public, under the terms of the agreement between the Company and the State and employee representatives, which was signed on the eve of the Company's privatization.

After these deposits, the "deficit" in the fund for eligible employees, as defined in the agreement between the Company, the State and representatives of the employees, which was signed on the eve of the privatization, was fully covered.

Note 5 – Legal proceedings

5.1 Class actions

In prior years, two legal and financial claims were lodged against the Company, which were recognized by the Courts in prior years as class actions:

- 5.1.1. In October 1998, a claim was lodged in Nazareth District Court against the Company, as well as a motion for recognition as a class action, in the amount of NIS 230.4 million (\$57.4 million as at the balance sheet date). The claim related to an allegation of overcharging for airline tickets by travel agents, which the plaintiff alleges were created by using improper exchange rates. In 2002, the Court recognized the motion to recognize the claim as a class action in the context of the Consumer Protection Law. The Company filed a motion for leave of appeal with the Supreme Court. In the Company's estimation, based on the opinion of its legal counsel, the Company is not expected to be found liable for this claim. A provision for this claim is not included in the financial statements.
- 5.1.2. In September 1999, a claim was lodged in Tel-Aviv District Court against the Company and against the Airport Authority and Ophir Tours (a travel agency), as well as a motion for recognition as a class action, in the amount of NIS 21.7 million (\$5.4 million as at the balance sheet date). The plaintiff alleges that the travel agency collected the passenger's fee from it using an exchange rate exceeding the legal rate for this purpose, which is the representative exchange rate, and that the Company is also responsible for the actions of the agents in this matter. In 2002, the Court approved the motion for class action recognition in the matter of breach of legislated duty based on Regulation 29 of the Civil Procedure Regulations. The Company filed a motion for leave of appeal with the Supreme Court.

El Al Israel Airlines Ltd.

Notes to the Condensed Consolidated Interim Financial Statements

Note 5 – Legal proceedings (continued)

In October 2005, a ruling was issued in the A.S.T. case, in which the Supreme Court ruled that class actions are possible only by virtue of specific legislation that includes this possibility, and that class actions may not be lodged in causes of action from the general law, by invoking Regulation 29 of the Civil Procedure.

Consequently, the parties were asked to submit their positions to the Court with respect to continuing the proceedings. The plaintiff announced that it wishes to continue the hearings based on a cause of action from the Consumer Protection Law, which was not approved in District Court. The Court has not yet ruled on this issue. In the Company's estimation, based on the opinion of its legal counsel, the Company is not expected to be found liable in this claim. No provision was included for this claim in the financial statements.

5.2 Anti-trust lawsuits abroad

5.2.1 In February 2006, the Anti-Trust Department of the U.S. Justice Department ("Anti-Trust Department") instituted an open investigation, together with other such authorities in other countries, for alleged suspicion of price fixing regarding certain increments in air cargo transport prices. Several cargo airlines announced that they had received grand jury subpoenas in connection with this investigation. On September 27, 2006, the Company received a grand jury subpoena from the Anti-Trust Department, demanding information and documents related to the pricing practice and to certain price increments related to flying cargo, from early 1999 until the subpoena date. The Anti-Trust Department informed the Company that the Company would be investigated as a suspect in this investigation. As such, no provision was recorded for this investigation. The Company is cooperating with the investigation, while performing an internal investigation of cargo pricing practices. At this stage, the Company is unable to assess the outcome of the Anti-Trust Department's investigation or the possible financial impact of the investigation. However, it should be noted that the implications could include administrative and/or civil proceedings, and/or a criminal indictment, including penalties and/or civil liability. It is also stated that the penalties for violation of Anti-Trust laws could be serious, with respect to the legal liability and the civil liability.

5.2.2 In December 2006, the Company received a letter from the European Anti-Trust Commission ("the Commission"), which was delivered to the Company's offices in Germany, demanding information in connection with the investigation being conducted by the Commission. The letter stated that the demand for information was within the scope of an investigation that the Commission is conducting with respect to activities that allegedly hurt competition in the air cargo transport services sector, and that the Commission has information on extensive contacts maintained between the airlines and other bodies pertaining to various price increments and other matters, such as the tariffs for cargo transport.

The letter asked the Company to transfer data and documents relating to the Company and its cargo activities since 1995. The Company is cooperating with the investigation and sent its response, as requested by the Commission's letter, while it is also conducting an independent internal examination of the cargo pricing practices. At this juncture, the Company is unable to assess the outcome of the Commission's investigation or to estimate the investigation's possible financial impact on the Company, and therefore, no provision for this investigation was included in the financial statements.

El Al Israel Airlines Ltd.

Notes to the Condensed Consolidated Interim Financial Statements

Note 5 – Legal proceedings (continued)

5.2 Anti-trust lawsuits abroad (continued)

However, it should be noted that the implications could include administrative proceedings against the Company, including a substantial penalty that could be imposed on the Company at the end of the process.

5.2.3 The proceedings detailed above, related to the investigations of Anti-Trust Authorities, could have a material effect on the Company, due to the penalties that these bodies are allowed to impose, and which could be particularly high.

5.2.4 In February 2007, the Company received a civil statement of claim that was filed in New York Court regarding the air cargo transport service prices.

The Company was added to the statement of claim as a defendant, alongside 38 other airlines, in which it is alleged that the defendants were partners in a price fixing arrangement for cargo air transport services since 2000, while violating the anti-trust and other laws in Europe and the U.S.

The claim was filed on behalf of the bodies purchasing the cargo air transport services, directly and indirectly, in Europe and the U.S., and includes a motion for recognition of the claim as a class action. The claim contains a motion for damages at an unspecified amount and for other relief.

The Company is examining the statement of claim submitted to it and its possible implications, and is preparing to deal with these proceedings. In view of the early stage of the process, the Company is unable to estimate its implications or the financial impact of the process on the Company. Accordingly, no provision was recorded for this claim in the financial statements.

5.3 Additional material claims during the current period

5.3.1 On January 22, 2007, a claim was filed against the Company in Jerusalem District Court, together with a motion for recognition as a class action, in the amount of NIS 483.4 million (\$120.5 million as at the balance sheet date).

The plaintiffs allege that the collection of a security fee of \$8 per flight leg, from passengers in flights that are not flown by the Company itself, but by other airlines under code sharing arrangements, constitutes misleading the consumer, breach of the agreement with him, the absence of good faith and unlawful enrichment, since, the plaintiffs allege, these flights do not provide security services at the same standard and quality as the services provided by the Company.

The plaintiffs are requesting that the Company be required to pay each of these passengers the sum of \$8 as well as damages of NIS 500 for emotional distress and loss of benefit.

In the Company's estimation, based on the opinion of its legal counsel, the Company is not expected to be found liable for this claim. A provision for this claim was not recorded in these financial statements.

El Al Israel Airlines Ltd.

Notes to the Condensed Consolidated Interim Financial Statements

Note 5 – Legal proceedings (continued)

5.3 Additional claims (continued)

5.3.2 On March 19, 2007, a claim was filed in Tel Aviv District Court against the Company, together with a motion for recognition as a class action. The plaintiff alleges that customers who purchase airline tickets directly (and not through travel agents), using credit cards, are charged in foreign currency instead of in Israeli currency, with a payment of a conversion fee of 2% of the price of the ticket (for conversion of the foreign currency payment into an Israeli currency payment) to the credit card companies, constitutes a violation of the Consumer Protection Law, 1981, a breach of the duty to act in good faith and unlawful enrichment. Also alleged was a violation of the obligation to advertise the "total price", and that it is the Company that needs to bear the conversion fees. Additionally, the plaintiff alleges that the charging of customers in foreign currency and not in shekels is by itself a violation of the Consumer Protection Law. The plaintiff is requesting that the Company be required to pay damages to every member of the class in the amount of all the conversion fees unlawfully collected and to issue an order against the Company stipulating that the collection of payments in foreign currency and the related charges of fees was unlawful, and to prohibit the Company from continuing to collect payments in foreign currency and to roll the conversion fee payments to its customers. In the Company's estimation, based on the opinion of its legal counsel, the Company is not expected to be found liable for this claim. A provision for this claim was not recorded in these financial statements.

5.4 Regarding the claim filed against the Company subsequent to the balance sheet date, see Note 8.2.

Note 6 – Other income and expenses

6.1 As a result of the discontinuation of operations of a company related to Boeing, with which the Company had an undertaking in the past to operate Internet systems on some of the Company's aircraft, the Company discontinued the providing of such service. In January 2007, an agreement was signed between the Company and Boeing, whereby the Company received damages from Boeing for its investments in the Internet system, and the additional damages it sustained due to discontinuation of the system's operation. As a result of these damages, the Company recorded income in the period of three months ended March 31, 2007 of \$4.4 million, which was charged to "other income".

6.2 In March 2007, the Company signed an agreement with the British Aviation Authority, whereby a property that had been used in Heathrow Airport in London was vacated, and accordingly, it received early vacancy fees from the above Aviation Authority.

As a result of this agreement, the Company recorded net income (after taxes) of \$3.4 million in the period of three months ended March 31, 2007, which was charged to "other income".

El Al Israel Airlines Ltd.

Notes to the Condensed Consolidated Interim Financial Statements

Note 6 – Other income and expenses (continued)

- 6.3** In July 2007, a clarification to an agreement between the Company and Boeing was signed, with respect to an overall accounting between the parties. Within this framework, there was agreement that the sum of \$6.5 million of the cash flows, which were or are expected to be received by the Company from Boeing constitute damages for the loss of revenues sustained by the Company due to the discontinuation of two joint projects, including the project for broadband Internet in planes. This amount was included in the Company's other income in the period of three months ended June 30, 2007.
- 6.4** Other expenses for the period of three months ended June 30, 2007 include a provision for the early retirement plan for an additional 60 employees, totaling \$6 million. Management expects that most of these employees will be included in the framework of early pension payments, and some will receive increased severance payments.

El Al Israel Airlines Ltd.**Notes to the Condensed Consolidated Interim Financial Statements****Note 7 – Operating segments**

Presented below is reporting according to geographic segments, on a consolidated basis:

	North America	Europe	Far East and Central Asia	Rest of the world	Total
	(in thousand US dollars)				
For the period of nine months ended September 30, 2007 (unaudited)					
Revenues -					
Revenues by segment	<u>500,975</u>	<u>611,846</u>	<u>240,472</u>	<u>30,070</u>	1,383,363
Revenues not allocated to segments					<u>24,793</u>
Total consolidated revenues					<u>1,408,156</u>
Operating income -					
Operating income by segment	<u>41,897</u>	<u>113,413</u>	<u>18,309</u>	<u>9,226</u>	182,845
Expenses of all segments, net					<u>(110,399)</u>
Consolidated operating income before financing expenses, net					<u>72,446</u>
For the period of three months ended September 30, 2007 (unaudited)					
Revenues -					
Revenues by segment	<u>204,678</u>	<u>256,741</u>	<u>85,546</u>	<u>11,070</u>	558,035
Revenues not allocated to segments					<u>8,680</u>
Total consolidated revenues					<u>566,715</u>
Operating income -					
Operating income by segment	<u>27,014</u>	<u>64,594</u>	<u>8,848</u>	<u>4,193</u>	104,649
Expenses of all segments, net					<u>(40,805)</u>
Consolidated operating income before financing expenses, net					<u>63,844</u>

El Al Israel Airlines Ltd.**Notes to the Condensed Consolidated Interim Financial Statements****Note 7 – Operating segments** (continued)

Presented below is reporting according to geographic segments, on a consolidated basis:

	North America	Europe	Far East and Central Asia	Rest of the world	Total
	(in thousand US dollars)				
For the period of nine months ended September 30, 2006 (unaudited)					
Revenues -					
Revenues by segment	<u>441,248</u>	<u>541,383</u>	<u>216,579</u>	<u>28,528</u>	1,227,738
Revenues not allocated to segments					21,012
Total consolidated revenues					<u>1,248,750</u>
Operating income -					
Operating income by segment (*)	<u>15,119</u>	<u>76,506</u>	<u>28,902</u>	<u>8,862</u>	129,389
Expenses of all segments, net					<u>(128,839)</u>
Consolidated operating income before financing expenses, net					<u>(*) 550</u>
For the period of three months ended September 30, 2006 (unaudited)					
Revenues -					
Revenues by segment	<u>162,443</u>	<u>192,963</u>	<u>73,378</u>	<u>10,781</u>	439,565
Revenues not allocated to segments					7,436
Total consolidated revenues					<u>447,001</u>
Operating income -					
Operating income by segment (*)	<u>9,459</u>	<u>30,573</u>	<u>4,641</u>	<u>3,873</u>	48,546
Expenses of all segments, net					<u>(40,024)</u>
Consolidated operating income before financing expenses, net					<u>(*) 8,522</u>
For the year ended December 31, 2006 (audited)					
Revenues -					
Revenues by segment	<u>580,399</u>	<u>702,909</u>	<u>313,500</u>	<u>36,590</u>	1,633,398
Revenues not allocated to segments					32,048
Total revenues					<u>1,665,446</u>
Operating income -					
Operating income by segment (*)	<u>14,937</u>	<u>84,119</u>	<u>39,535</u>	<u>7,989</u>	146,580
Expenses of all segments, net					<u>(155,050)</u>
Operating loss before financing expenses					<u>(8,470)</u>

(*) Restated - see Note 1.5.

El Al Israel Airlines Ltd.

Notes to the Condensed Consolidated Interim Financial Statements

Note 8 – Subsequent events

- 8.1 On October 7, 2007, the Company's board of directors resolved to distribute a dividend totaling NIS 0.075 per ordinary share, NIS 1 par value. The total dividend amount (based on the exchange rate on that date) is \$9,265 thousand. The dividend was actually distributed on October 29, 2007.
- 8.2 In November 2007, a claim was lodged in Haifa District Court against the Company, as well as a motion for recognition as a class action pursuant to the Class Action Law, in the amount of NIS 105 million (\$26 million as at the balance sheet date). The plaintiffs claim that the prices charged by the Company for overweight baggage on its flights are excessive and calculated without any connection to the Company's ordinary flight prices. The Company is studying the claim and is preparing to file its response.
- 8.3 On November 20, 2007, the Company's board of directors resolved to publish an additional outline for the purpose of allotting options that are located in the reserve of options available for allotment, in accordance with the option plan for compensation of managers and other employees of the Company, the balance of which as at such date is 3,382,843 options. The options will be exercisable for up to 3,382,843 ordinary shares, NIS 1 par value of the Company.

The board of directors approved the appointment of a Human Resources and Appointments Committee to continue serving as the option plan administrator, and empowered the committee to allot the above options to the Company's managers, in accordance with the criteria provided by the board of directors.

The theoretical exercise price of each option will be 85% of the average closing price of an ordinary share of the Company on the Tel Aviv Stock Exchange during the 30 trading days that preceded the decision of the plan administrator for an allotment to each offeree.

The options will not be listed for trading, although the underlying shares from the exercise of the options will be listed for trading on the stock exchange.

The options will be allotted on the capital gains track with a trustee, under Section 102 of the Income Tax Ordinance.

The options will be distributed in four equal installments that will vest in four installments, as follows: one-quarter will vest on July 1 of each of the years 2008 through 2011, inclusive.

The exercise price will be the theoretical price that is not paid by the employee. If the option is exercised, the employee will be eligible for a number of shares equal to the difference between the price of the underlying share (the closing price of an ordinary share on the Tel Aviv Stock Exchange at the end of the trading day on which notice of exercise was submitted to the Company), and between the theoretical exercise price, multiplied by the number of options held, divided by the exercise price of the share.

The theoretical exercise price is subject to customary adjustments in the event of a dividend distribution and changes in the composition of the Company's capital.

Pursuant to the provisions of Accounting Standard No. 24 (Share-Based Payment) of the Israel Accounting Standards Board, the Company will record expenses for the granting of the options based on their economic value. The calculation will be made on the grant date, separately for each installment, according to the Black & Scholes model. The expense will be recorded over the vesting period of the installment, with the amount of the expense being a function of the number of options granted and the economic value of each option.

At the date of the board of directors' resolution on the issuance of the outline, the calculation of the expenses that the Company will bear for the value of the benefit in this plan is \$0.9 million.