

EL AL ISRAEL AIRLINES LTD.

FINANCIAL STATEMENTS AS OF SEPTEMBER 30, 2008 (unaudited)

CONTENTS

SECTION A - UPDATE OF CHAPTER A TO 2007 ANNUAL REPORT

SECTION B - DIRECTOR'S REPORT

SECTION C - FINANCIAL STATEMENTS

Update to Chapter A (Description of Corporate Business)¹
to the 2007 annual report ("periodic report")
of EL AL Israel Airlines Ltd. ("the Company")

1. Description of general development of Group business

Starting in the first quarter of 2008, the Company has begun preparing its Financial Statements in accordance with International Financial Reporting Standards (IFRS).

As a result of the shift to IFRS reporting, the Company has presented its Financial Statements for the reported period as well as comparative numbers for the same period last year and for the year ending 2007 in accordance with IFRS.

As for the accounting implications and adjustments required as a result of the shift to IFRS reporting, see Note 9 of the Company's Financial Statements dated September 30 2008.

The following is data prepared in accordance with the IFRS, which appeared in Chapter A - Description of the Corporation's Business for the 2007 Periodic Report, as required by the Securities Authority (FAQ 1).

Note that according to the transfer guidelines to IFRS reporting, 2005 and 2006 data need not be presented anew.

To item 5 - Financial Data Regarding the Corporation's Areas of Activity

2007:

	Passenger aircraft (Thousands of Dollars)	Cargo aircraft (Thousands of Dollars)	Others and adjustment to consolidated (Thousands of Dollars)	Total (Thousands of Dollars)
Passenger revenues	1,547,505	-	-	1,547,505
Cargo and mail revenues	106,217	216,338	-	322,555
Other revenues	38,692	994	22,704	62,390
Total revenues	1,692,414	217,332	22,704	1,932,450
Costs	(1,567,319)	(255,344)	(15,114)	(1,837,777)
Operating income (loss)	125,095	(38,012)	7,590	94,673
Fixed assets at year end	1,196,726	42,467	46,559	1,285,752

¹ This update is in accordance with Regulation 39a of the Securities Regulations (Periodic and immediate reports), 1970 and includes material changes or additions which have occurred in corporate business on any matter which is to be described in the periodic report. The update refers to item numbers in Chapter A (Description of Corporate Business) in the Group's 2007 annual report.

To item 7.3 – Income Segmentation and Service Profitability in the Area of Passenger Aircraft

	2007	*2006	* 2005
Gross profit (in thousands of dollars)	416,626	240,063	354,211
Gross margin (%)	25%	17%	25%

* Data for 2005 and 2006 was re-stated due to change in Company revenue distribution between passenger operations and cargo operations.

To item 8.3(b) – Income Segmentation and Services Profitability in the Area of Cargo Aircraft

	2007	*2006	*2005
Gross profit (in thousands of dollars)	(13,346)	17,821	10,622
Gross margin (%)	(6%)	8%	5%

* Data for 2005 and 2006 was re-stated due to change in Company revenue distribution between passenger operations and cargo operations.

To item 9.4.8 – Pension agreements

Below are details of Group long-term liabilities as regards employee benefits (consolidated data, in thousands of dollars):

	December 31, 2007 (Thousands of Dollars)
Employee severance pay liabilities and pension funds	179,725
Less - compensation and pension funds	(200,518)
Liabilities resulting from unutilized sick days, retirement bonuses, jubilee bonuses and retirement adjustment payments	37,336
Liabilities resulting from early retirement plans, net	40,029
Less – current maturities	(1,821)
Total	54,751

To item 9.6.5 – Working capital Deficit

As of December 31, 2007, the Group had a working capital deficit amounting to \$150 million compared to \$204 million at the end of the previous year. The Company's current ratio at the end of 2007 is 77%, compared to 65% at the end

of the previous year. For details of the causes for decrease in working capital deficit, see item 2.1 of the Board of Directors' report for 2007.

The following are additional updates to Chapter A – Description of corporate business:

To item 3.4 – Changes in holdings of interested parties

El-Al Employee Holdings in Trust Ltd. (hereinafter: "**the Employee Holding Company**"), a Company interested party, reported to the Company several sales of shares (as reported by the Company). After the performance of the above transactions, the Employee Holding Company holds 31,198,700 shares which constitute 6.29% of the Company's issued and paid-up capital.

Mr. Pinchas Ginsburg, an interested party in the Company, conducted multiple transactions to buy and sell shares (as reported by the Company). As of November 13 2008, following the aforementioned transactions, Mr. Ginsburg owns, in his name and on behalf of other individuals in the Ginsburg Group, 38,676,823 shares which constitute 7.80% of the Company's issued and paid-up capital.

As reported by the Company, on September 24 2008 A.L. Aviation Assets (hereinafter: "**A.L. Aviation Assets**"), a privately-owned company the issued capital of which is held in equal portions by Lenders' Assets Ltd., a Company controlled by Yehuda (Yudi) Levi, a Company director, and Miella Venture Partners, a company fully owned by a foreign-based trust the beneficiaries of which are the members of the Effi Arzi family, became an interested party in the Company. A.L. Aviation Assets conducted several purchases and sales of shares (as reported by the Company).

As of November 13 2008, after conducting several purchasing activities, A.L. Aviation Assets holds 1,363,668 shares which constitute 0.28% of the Company's issued and paid-up capital.

2. General environment and impact of external factors on the corporation

To item 6.1 – Traffic in the international airline industry

Over recent months, and even more so over the past few weeks, the world has been experiencing an unprecedented financial crisis. The crisis, which originated in the U.S., has influenced markets both in Europe and in Asia. We have seen share markets fall across the west, East Asia and in Israel, as well as the collapse of some financial bodies and the nationalization of others. This crisis is expected to lead to a global slowdown and possibly even a recession.

This situation originated with the sub-prime crisis, which began in the second half of 2007 and which hurt world banks and financial markets with significant exposure to sub-prime loans via debt instruments backed by these loans. As a result, and particularly starting from the third quarter of 2008, global capital markets suffered from major upheavals, which on the one hand included

financial institutions and companies becoming insolvent, and on the other hand saw attempts on behalf of central banks around the world to pump liquidity into banking systems while lowering interest rates in order to curb the effects of the crisis.

The global financial crisis has had a significant effect on the airline industry as well. Since the beginning of the crisis, some 25 different airlines have announced major financial difficulties (up to and including liquidation), and factors in the airline industry estimate that this number will increase significantly by the end of the year. The main reasons for this are the material increase in fuel expenses, the share drop in demand and the diminished willingness of financing bodies to finance members of the airline industry.

Note that most airlines terminating their operations have been relatively small. Nevertheless, the crisis has not passed over large airlines in financial difficulties, and high fuel prices and low demand has pushed them close to the edge.

Thus, for instance, the Italian airline Alitalia filed a request for bankruptcy protection from an Italian court in August 2008. This, after years of losses and government bailouts. This step was intended to pave the way for the company's breakup and re-launch by a consortium of Italian investors. The company currently operates 17 weekly flights on the Israel-Rome or Milan routes.

The Greek government has also announced that it would be partially privatizing Olympic Airways, the Greek national carrier. This step takes place after the company entered severe financial difficulties, and received the EU's approval to conduct a re-organization program. This, following several failed attempts made by the Greek government to sell the company to an outside party.

In November 2008, Corsair Airlines, from the TUI Group, discontinued its regular flights in the Winter 2008/9 period between Tel Aviv and Paris due to a lack of financial viability, this after receiving second Designated Carrier status on behalf of France for the Tel Aviv-Paris line. According to press publications, Corsair intends to renew its flights on this route throughout March 2009, with the commencement of the summer schedule.

On the other hand, in light of the deepening financial crisis in the U.S., its expansion to other world markets and fears of a global recession and a drop in the demand for petroleum and petroleum products, over recent weeks we have seen sharp and continuous drops in fuel prices. Oil prices have dropped by over 60% since peaking at \$147 per barrel on July 11 2008. As of the publishing of this report, the price of future oil contracts for delivery in December has dropped to under \$55 per barrel.

According to IATA² data, September 2008 saw a 2.9% decrease in international passenger travel compared to September 2007. Load factors for international flights have dropped to 74.8% from 79.2% in August 2008.

Passenger travel has decreased for the first time since the SARS epidemic in 2003, and even the sharp drop in fuel we've seen over recent months cannot compensate for the drop in demand. According to the president of IATA, taking this trend into consideration, airline losses may be even higher than the previous IATA projection, as published in early September 2008, and which predicted losses equaling \$5.2 billion for the airlines in 2008.

A 3.3% increase in international passenger travel occurred in the accumulated January-September 2008 period in comparison to the same period last year.

Data published by the American company OAG³, which deals in air transport information, indicates that airlines around the world will cut 451 thousand flights (consisting of a 6.1% decrease compared to Q4 2007) and 43 million seats (a 5.2% decrease in passengers compared to the same quarter last year) in the last quarter of the year as a result of the global economic crisis, this following a drop in vacation demand and business travel, particularly in the U.S.

Cargo:

In September 2008, the field of international air cargo dropped by 7.7% compared to September 2007. This is the sharpest drop in cargo movement since 2001.

The most significant drops in cargo movement were noted by East Asian airlines, which reported a 10.6% decrease in cargo movement in September 2008 compared to September last year.

European and North American airlines, which so far have seen low growth rates in their cargo movements, noted a 6.8% and 6.0%, respectively, decrease in cargo movement in September.

The decreases in cargo movement have slowed down the cumulative growth rate (January-September 2008) to a mere 0.1%, compared to the same period last year.

To item 6.2 – Traffic in the Israeli airline industry

According to data from the Central Bureau of Statistics, in July-September 2008, some 590 thousand tourists entered Israel by air - an 18% increase over the corresponding period last year. Furthermore, this quarter saw 1.3 million Israelis leave the country by air, a 1% increase over the corresponding period last year. It must be noted that this year, the holiday period fell in October

² IATA Press Release No. 49, October 24 2008. IATA data refers only to regular international flights. Domestic flights are not included. All data is preliminary and represents airline reports received by publications, along with IATA estimates regarding missing information

³ OAG Website, press release, October 10,2008

(which is in the fourth quarter), while last year the holidays fell in September.

Passenger movement through Ben Gurion Airport increased by 6% throughout this period compared to the same period last year, including on routes on which the Company does not operate flights.

Airport Authority data indicates that a 4.2% decrease occurred throughout the third quarter in air cargo movement to and from Israel, compared to the same period last year.

To item 6.3 – Fluctuations of jet fuel prices and to item 9.5.1 – Raw materials and suppliers - fuel

In the quarter ended September 30, 2008, market prices of jet fuel rose by 64% over the corresponding period last year. The average price of jet fuel for the Company, after hedging, increased by 67% over the same period last year. In this quarter, fuel expenses constitute 35% of turnover (27% in the third quarter of 2007). The information below regarding market prices refers to prices of jet fuel in the Mediterranean Region, as quoted by Platts⁴. For further information, see items 6.1, 6.2 and 6.5 of the Board of Directors' report on the state of corporate affairs.

The Company purchases fuel from four suppliers in Israel, chosen by open bid. In the quarter ending September 30 2008 the Company purchased some 35% of its fuel purchases for the quarter from a single supplier (the Paz Company).

On September 30 2008 the Company held jet fuel reserves, purchased from suppliers in Israel and abroad, to the amount of \$8.4 million.

To item 6.4 – Fluctuations in foreign currency exchange rates

Group financial results are affected by several currencies. Fluctuations in USD exchange rates vs. other currencies may improve or erode Group profitability.

As of September 30, 2008, the USD/NIS exchange rate declined by 14.8% compared to September 30, 2007, and declined by 11.1% compared to December 31, 2007.

As of September 30, 2008, the USD/Euro exchange rate declined by 3.0% compared to September 30, 2007, and increased by 0.7% compared to December 31, 2007. For further information, see item 3.4 of the Board of Directors' report on the state of corporate affairs.

⁴ To the best of the Company's knowledge, Platts Corporation is a member of the McGraw-Hill Group, and has been providing information about the energy industry for over 75 years. The Company provides current information and analysis, *inter alia*, with regard to prices and international events in the oil, petro-chemical, natural gas and electric & nuclear power markets.

To item 6.5 – Fluctuations in interest rates

In order to finance aircraft acquisitions, the Company has obtained material loans at adjustable interest rates based on LIBOR rates. Changes in LIBOR interest rates may materially impact the Company's financing expenses.

In the quarter ended September 30, 2008, the average 3-month LIBOR interest rate increased by 5.7% compared to the second quarter of 2008, while declining by 46.5% compared to the corresponding period last year. For further information, see item 6.3 of the Board of Directors' report on the state of corporate affairs

3. Passenger aircraft operating area

To item 7.1.5 - Technological changes that may materially impact the operating area

Pursuant to items 7.1.5 and 7.6.2 of the annual report and the report for the first and second quarters of 2008 with regard to transition of the Company to using the AMADEUS reservation system, in the third quarter of 2008, as part of the implementation of Phase II of the transition to the AMADEUS reservation system, preparations began for the implementation and assimilation of the new DSG model (Airport service system).

In addition, an agreement was signed with Lufthansa Systems in Q3 2008 for the receipt of optimal flight route planning services, taking fuel and tax costs into consideration.

In addition, over the course of Q3 2008 the Company began studying technological solutions for the sale of ingoing and outgoing tourism services, as a part of its website and direct sales points.

To item 7.1.10 - Competitive Structure in Areas of Activity and Changes Therein

As part of its flight array optimization strategy, the Company discontinued its direct flights to Miami starting September 2008, this in light of this route's lack of viability. In addition, the Company announced that it would be changing the format of its activity on the Minsk route (see update to item 7.4 below).

In light of recent drops in fuel prices, the Company announced that it would increase seat availability on its direct flights to business destinations in the Winter 2008/2009 period. The increase in seat availability shall be by adding 11 weekly frequencies to European destinations. Starting late October 2008, the Company added two weekly flights to destinations in Barcelona, Milan, Rome, Prague and Bucharest as well as an additional weekly flight to Sofia. In addition, the Company began operating a Boeing 777 aircraft on the Mumbai route starting November 2 for the winter period, for business travelers.

- In late September 2008 Korean Air began operating 3 weekly flights on the Tel Aviv-Seoul route.
- In August 2008, US Airways announce that it intended to operate direct flights between Philadelphia and Tel Aviv starting July 2009.
- Starting September 2008, Iberia Airlines increased its weekly seat capacity by 13% for the Tel Aviv-Madrid route, after entering an A340 aircraft into service for two of its 14 weekly flights.
- For the first time, Arkia Airlines received Ministry of Transport approval to operate a regular flight route between Tel Aviv and Kiev. Arkia's appointment as second Designated Carrier occurred following the new aviation agreement between Israel and Ukraine, signed July 2008, which permits the appointment of two Designated Carriers for this route.

On the other hand, the U.S. financial crisis, which has been spreading to the rest of the world, combined with high fuel prices which were the cause of a severe crisis in the airline industry, have started to affect the Israeli markets and to the best of the Company's knowledge, have led to the following occurrences:

- Israir has discontinued its regular flights on the New York route starting middle September 2008 and has announced that it intends to reduce its charter activity on the London route for the winter period, despite receiving additional Designated Carrier status for this route from the Ministry of Transportation.
- In September 2008, the Kazakhstan airline (Sayakath) announced that it would be discontinuing its flights to Israel.
- Air Lithuanian (Lithuania), which operated flights between Vilnius and Tel Aviv, discontinued its flights in August.
- In September XL, Britain's third largest tourist company, specializing in charter flights and vacation sales, declared bankruptcy. The Company, which operated flights to Israel from France and the U.K., discontinued its activity immediately.

Pursuant to item 7.1.10(b) of the periodic report, in accordance with the "open sky" policy held by the Israeli Ministry of Transportation, a new aviation agreement ("horizon agreement") was signed in August 2008 paving the way for the establishment of a global aviation agreement between Israel and the EU. In addition, an agreement was reached between the parties for the establishment of the framework and content of the negotiations for the global aviation agreement.

Pursuant to item 7.1.10(b) of the periodic report, on August 24, 2008, Government Resolution no. 4032 was passed on the subject of the state's participation in Israeli airline security expenses, as follows:

1. *"To revoke Government Resolution no. 3024 dated January 27 2008 (hereinafter "the Resolution") starting January 1 2009 or on the date on which the scope of passengers entering and exiting Israel by air is greater than 10.7 million passengers per year, whichever is later.*
2. *Section A of the Decision shall be implemented until its cancellation as stated in Section 1 of this decision, only on flight routes for which an additional listed Israeli carrier has been actively appointed, which has started to operate on the flight route.*
3. *To authorize the Ministries of Finance and Transportation and Road Safety to increase the state's participation rate in security costs for Israeli airlines, pursuant to the signing of a global aviation agreement with the EU in accordance with Government Resolution no. 441 dated September 12 2006.*
4. *The budgetary expense of Government Resolution 3024, until its cancellation as denoted in Section 1, shall be financed from the Ministry of Transportation's existing budget."*

The Company's position is that both levels of Government Resolution 3024 (changing flight policy on regular routes in the matter of the appointment of a Designated Carrier and the increase in the participation of security expenses of Israeli airlines) must be upheld. For details, see update for Section 9.11.12 below regarding the Company's petition to the High Court of Justice.

The Company's assessment with regard to increased expenses due to enactment of the aforementioned legislation may constitute forward-looking information, as defined in the Securities Act, based on Company assumptions and forecasts. Therefore, the actual outcome of enactment of the aforementioned legislation amendment or the extent of its impact, if enacted, on Company operations may materially differ from the outcome expected or implied by this information.

Pursuant to item 7.1.10(c) of the periodic report, American Airlines, British Airways and Iberia have increased their cooperation. In August 2008 the three companies signed a commercial cooperation agreement for all matters related to flights between the U.S., Mexico, Canada, the EU, Switzerland and Norway ("the Agreement"), while continuing to act as separate bodies. The three companies intend to expand their code share agreements for flights inside and outside Europe and the U.S., allowing passengers to choose a shared network of the three airlines. To the best of the Company's knowledge, this agreement is also expected to help the Oneworld alliance, of which the three airlines are members, compete more efficiently with other aviation alliances. At the same time, according to press publications, Lufthansa, which constitutes the lead element of the "Star Alliance" airline alliance, announced that it would be purchasing the British airline BMI circa January 2009, thus becoming Europe's largest airline, this by way of response to the activity described above. This purchase shall allow the German airline to receive reserved arrival and departure slots in Europe's most active airport – Heathrow, this in light of the fact that BMI is Heathrow's second most active airline, holding 12% of all reserved slots at this airport. Such a step may provide the German airline with a great deal of flexibility for its flights to the U.K., and from there to further destinations in North America

Pursuant to item 7.1.10(d) of the periodic report and the updates for the first and second quarters of 2008, the third quarter of 2008 saw a 6.3% increase in total passengers at Ben Gurion airport compared to the same period last year, with operations of scheduled airlines growing by 10.7%, while operations of charter airlines dropped by 3%. Passenger traffic in Ben Gurion airport for the quarter broke down as follows: the Group – 32.2%, other regular companies – 43.4%; other charter companies – 24.4%.

The capacity of foreign regular companies (including regular Arkia and Israir flights) has increase by 27% over the course of the quarter and the amount of passengers has increased by 24% compared to the same quarter last year, this mainly in light of the fact that:

- Turkish Airline has increased the weekly frequencies of its flights on the Tel Aviv-Istanbul route from 18 to 25 (a 23% increase in seat availability) starting Q2 2008.
- Delta Airlines, which listed an 84% increase in its seat capacity, after it started operating a daily flight on the New York route in March 2008 in addition to its flights on the Tel Aviv-Atlanta routes, has increased its weekly frequencies from 7 to 14.
- Air Canada has increased its frequencies on the Toronto route from 5 to 7 (a 33% increase in seat availability).
- The Czech airline has increased its frequencies on the Prague route from 7 to 11 per week (a 60% increase in capacity).
- Transaero, from Russia, operated at frequencies of 17 per week compared to 14 or the comparative quarter last year on the Moscow route.

This while El Al has reduced its ASK by 6.3% and its passenger activity has dropped by 5%.

To item 7.2 – Services in operating area, to item 7.4 – New services

The Company launched a new service in August 2008 granting passengers flying economy class the option of premium seating, this in return for additional payment and/or frequent flier points. Premium seating is a seat with improved legroom, adjacent to exits or partitions.

The Company began charging service fee for changes in flight tickets and the sale of flight tickets using avenues of sales not via travel agents.

In October 2008 the Company signed a code share agreement with Belavia-Belarusian Airlines (hereinafter: "**Belavia**"). According to the agreement, which is a "soft block" type agreement, El Al shall receive a seat allotment on flights operated by Belavia, which shall operate between 2 and 5 weekly flights on the Tel Aviv-Minsk line, based on the seasonality of traffic. The flights shall operate in an economy class-only configuration. This agreement shall go into

effect on November 30 2008, subject to approval by Israeli and Belarusian authorities.

To item 7.11 – Aircraft fleet in the area of passenger aircraft activity

Pursuant to that denoted in 7.11 of the update to the periodic report for the second quarter of 2008, as reported by the Company, delivery of one of the 767-200 aircraft to an airline in the Philippines was completed on October 15 2008, this after the full price of the plane, amounting to \$6.5 million U.S., was paid to the Company immediately prior to signing the agreement. Regarding the sale of the second 767-200 aircraft, the intended purchaser, a Singapore investment company, informed the Company that it would be unable to meet payments for the aircraft as a result of difficulties in securities bank financing and therefore would be unable to purchase it, with the advance payment to the amount of \$325 thousand remaining in the Company's possession. The Company charged a pre-tax capital gain to the amount of \$4.7 U.S. in its Q3 Financial Statements for the sale of the aircraft in question. For details see Item 4d of the September 30 2008 Financial Statements.

Pursuant to item 7.11(a) of the periodic report regarding the agreement for the purchase of four 777-200ER aircraft from the Boeing Corporation, the Company reached an agreement with Boeing that the final date for the Company's decision regarding the option granted the Company by Boeing to convert the aircraft in question to 777-300ER configuration shall be deferred to February 25 2009.

The Company has continued its renewal, which includes purchasing of new aircraft for long and short routes, upgrading of the Company's aircraft and rejuvenating its fleet:

- A new 737-800 aircraft joined the Company's passenger fleet in August 2008, the first of five planes of this model intended for the El Al fleet. The aircraft was leased for an 8 year period and contains 142 seats. An additional new aircraft of this model was planned to be delivered to the Company in October 2008, but as a result of a strike at Boeing, the plane's manufacturer, its delivery to the Company was postponed. The Company plans to receive an additional three aircraft of this model in the first few months of 2009.
- Following Item 7.11(a)(3) of the periodic report, the Company received a 747-400 passenger plane, manufactured in 1994, which was purchased by the Company, in October 2008.

4. Cargo aircraft operating area

To item 8.1.3 (a) – Global cargo transport volume

According to reports by IATA, January-September 2008 saw a mere 0.1% increase in global cargo transport volume by cargo airplane over the corresponding period in 2007, i.e. a growth rate lower than expected by IATA

estimates (5%). This stalled growth is a result of a decrease in air cargo activity in Asia and South America, primarily Brazil. Nevertheless, we are unable to estimate whether this data changes expectations as to the overall annual growth rate for 2008.

According to data from the Airport Authority, January-September 2008 saw a 2.2% increase in cargo transport volume by cargo aircraft at Ben Gurion airport (following a 4.4% drop in the third quarter), compared to the corresponding period in 2007, while IATA forecasts called for a 4.8% annualized growth rate.

To item 8.2 – Services in operating area

A process was completed on October 6 2008 according to which cargo transport in Europe was concentrated at the Liège, Belgium airport, which constitutes a single central airport, as an alternative to distributing cargo activity throughout three Benelux airports. The chief advantages of the move to Liège Airport are:

- A lack of noise restrictions for activity hours which allows the establishment of an appropriate and fixed timetable for customers and a greater deal of flexibility.
- A location in the center of Europe and access to a broad continental shipping network.
- Logistic exclusivity for cargo shipping purposes.
- The airport offers customs and veterinary services for the agricultural sector, 24 hours a day, 7 days a week.
- Flight time to Tel Aviv is 40 minutes shorter than the flight to the Amsterdam station, where most cargo activity had been located previously.

Note that the Amsterdam station shall remain a center of activity and collection point even after the shift to Liège.

The shipping service provider that shall provide El Al with storage and operating area services as well as customer service is a new shipping company operating out of Liège – Liège Handling Services S.A., jointly owned by Avia Partner, owner of a network of 32 shipping stations in Europe, including in Belgium, France, Germany and the Netherlands (51%), the Liège Airport management (24.5%) and the four managers of the airport's cargo terminal (24.5%).

To item 8.7 – Competition

The Group estimates that its share of air cargo shipping throughout January-September 2008, out of total air cargo flown to and from Israel (including cargo flown onboard passenger aircraft and mail operations, except for cargo flown on sixth freedom operations) stood at 33.2%. The decrease in Company share of cargo transport is primarily due to the decrease in agricultural exports and to discontinuation of EL AL cargo aircraft flights to the Far East starting in May 2008 (as stated in Item 8.2 of the Company's periodic report for Q1 2008).

To item 8.10 – the Aircraft Fleet

Pursuant to item 8.10 of the periodic report, Cargo Division intends to shift to activities using only two 747-200 cargo planes. The Company approached the special state shareholder for approval, as instructed by the Company's Articles.

5. Details concerning the two areas of activity

To item 9.4.1 – Organizational Structure

Pursuant to that stated in Section 9.4.1 of the periodic report, a new department was established - the Purchasing and Commitment Department – under the supervision of the VP of Human Resources and Administration, in August 2008. The department shall concentrate all of the Company's purchasing activities.

To item 9.4.7 – special collective agreements

Pursuant to item 9.4.7 of the periodic report, the collective work agreement was signed on December 2 2008 by the Company, the employee representative and the Histadrut ("the Agreement"), after being approved by the Company's Board of Directors on October 27 2008. The primary points of this agreement are as follows:

- The Agreement shall be in effect until December 31 2012.
- Industrial peace and discipline - a commitment exists to uphold industrial peace for the duration of the agreement, while focusing on competition and growth challenges. The Company, the Histadrut and the employees' representatives shall conduct joint activities to promote and maintain order and discipline in the Company. The Company's authority as regards the termination of employees guilty of severe disciplinary violations shall be expanded.
- Bonuses and pay raises – when the Company becomes profitable, a general pay raise shall be granted equal to 3% of their pension salaries. In the event of profits greater than \$10 million, employee shall receive a one-time bonus equal to between 18% and 24% of their base salaries. In addition, in the following year, if the Company earns over \$10 million, an addition raise equal to 1% of pension salaries shall be granted. If the Company earns over \$35 million, an additional 0.5% shall be added to salaries. In the following year, if the Company earns over \$10 million, an additional 1% shall be added to pension salaries. If the Company earns over \$35 million an additional 0.5% shall be added.
- Horizon promotion bonus – when the Company becomes profitable, an annual budget for the financing of a horizon promotion bonus for non-promoted ground personnel as well as for flight crews and flight attendants with similar status. Non-promoted employees are workers who have spend many years at the top step of the existing standard pay scale and are not designated for promotion.

- Work cessation – initiated retirement and/or work cessation of 30 employees via a process including work cessation pathways using an increased compensation format, early pension or a choice between the above (in accordance with the retiring worker's age).
- Shifts and rest periods – shifts in Israel station and maintenance shall be adjusted and reinforced according to activity loads. Rest periods for pilots and regular and temporary flight attendants in North America shall be shortened.
- Special tracks and promotion – temporary employees with more than 3 years seniority may participate in bids for entry-level managerial positions. The Company shall be permitted to employ up to 40 employees via personal contracts. Employees in the flight technical files shall receive tenure after their fourth year instead of their second.

To item 9.4.16 – Executives and senior management

Pursuant to item 9.4.16 of the update to the periodic report for the first quarter of 2008, as reported by the Company on September 1 2008, Knafaim Holdings Ltd., the controlling shareholder of the Company (hereinafter: "Knafaim"), reported that it received two messages that morning from David (Deddi) Borowitz and Israel (Izzy) Borowitz, Knafaim controlling parties. The following are the messages, verbatim:

Mr. David (Deddi) Borowitz's message to Knafaim: "Following my letter to you dated May 27 2008, I hereby inform you that, at this stage of the negotiations between myself and my brother, Israel (Izzy) Borowitz, regarding the matter at hand [the option to purchase my brother Izzy Borowitz's shares in Knafaim], has not been signed, and the purchase agreement has not yet been completed."

Dr. Israel (Izzy) Borowitz's message to Knafaim: "I hereby inform you that, in spite of the fact that in May 2008 Deddi Borowitz announced that he would be exercising the option I granted him for the purchase of my shares in Knafaim and despite the fact that an agreement has been signed on the matter between Deddi and myself, according to which the final date for him to carry out the agreement was August 31 2008, Deddi failed to meet the terms of the agreement and the agreement was not carried out by him. In light of this fact, I shall continue with all my duties at El Al and Knafaim."

As reported by the Company on October 2 2008, on that very day the Chairman of the Company's Board of Directors, Dr. Israel (Izzy) Borowitz announced that he would be resigning his position as Chairman of the Board, starting November 30 2008 (Dr. Borowitz will continue to serve on the Board of Directors).

The Company also reported that the following had been decided in that day's meeting of the Board of Directors:

- (a) To appoint Mr. Amnon Lipkin-Shahak, a Company director, to the post of

- Temporary Chairman of the Board starting December 1 2008 until a permanent Chairman is appointed;
- (b) To appoint Mr. Yehuda (Yudi) Levi, a Company director, to the post of Vice Chairman of the Company's Board of Directors (in addition to Ms. Tamar Moses, serving as Vice Chairperson);
 - (c) To act to appoint Mr. Amikam Cohen as a director on the Board.

Pursuant to item 9.4.16 of the update to the periodic report for the second quarter of 2008, on November 19 2008 the Company shareholders' general meeting confirmed the appointment of Dr. Yehoshua (Shuki) Shemer as an outside director.

To item 9.10.3 – airport noise regulations

Over the course of the last quarter, the Company has commenced removing overly noisy aircraft from the roster of planes operated by the Company, in accordance with the El Al 2010 plan.

To item 9.11 – limitations on and supervision of the corporation's business

In November 2008 the Company discovered that following a review held by the American FAA at the Israeli Civil Aviation Administration, the FAA informed the Israeli Ministry of Transportation of its intention to announce that it would be lowering the State of Israel's aviation safety rating to Category 2. The above followed a visit by an FAA delegation to Israel to test the status and air safety supervision capabilities of the Civil Aviation Administration in the Ministry of Transportation.

To be clear, this review of safety ratings is not a result of the capabilities or the safety records of Israeli airlines, however, the effects of the rating decrease may harm the Company, including freezing of bilateral agreements and the inability to alter existing agreements; freezing commercial agreements without the possibility of submitting requests for added frequencies, adding flight times, changing destinations or receiving new flight destinations; freezing airlines' operational operator's licenses and the inability to add or integrate new aircraft on these routes; damage to code sharing agreements; careful testing of planes arriving from Israel to the U.S, which may lead to significant delays in planned flight times. The Company approached the Minister of Transportation with a request to act to prevent the announcement in question.

The Company's assessment with regard to increased expenses due to enactment of the aforementioned legislation may constitute forward-looking information, as defined in the Securities Act, based on Company assumptions and forecasts. Therefore, the actual outcome of enactment of the aforementioned legislation amendment or the extent of its impact, if enacted, on Company operations may materially differ from the outcome expected or implied by this information.

To item 9.11.2 – Regulatory arrangements

Pursuant to the update to the periodic report for the second quarter of 2008, the Ministry of Transportation presented the Company with a proposed amendment to the Airport Authority Regulations (Fees), which is to be presented by the Government to the Knesset's Economy Committee, involving a significant increase in outgoing passenger fees as well as fees payable by airlines operating out of Ben Gurion airport, including the Company, by an average increase of 51%. The Company and the various airlines operating at Ben Gurion Airport, the Foreign Airline Panel and IATA expressed their objection to the proposed amendment, and discussion on this matter has yet to be concluded. Adoption of the proposed amendment, as it currently stands, may negatively impact the Company's financial results due to the increased expenses for fees and services as a result of the aforementioned increase. To the best of the Company's knowledge, the Ministry of Transportation intends to present the Knesset Economic Committee with an amended proposal, formulated in conjunction with the Ministry of Transportation, the Ministry of Finance and the Airport Authority according to which the fee increase shall be at a lower rate. At this stage the Company cannot estimate the chance of its passing, its influence or the changes relative to the original proposal.

The Company's assessment with regard to increased expenses due to enactment of the aforementioned legislation may constitute forward-looking information, as defined in the Securities Act, based on Company assumptions and forecasts. Therefore, the actual outcome of enactment of the aforementioned legislation amendment or the extent of its impact, if enacted, on Company operations may materially differ from the outcome expected or implied by this information.

Pursuant to item 9.11.2(i)(1) of the periodic report, on October 30 the Ministry of Industry confirmed the type exemption for binding agreements between air carriers, signed by the Restraint of Trade Controller, the type exemption (Amendment 10 to the Restrictive Trade Practice Law) is supposed to come into effect on January 1 2009, and shall revoke the statutory exemption granted today to arrangements between air carriers regarding international shipping. As part of the amendment, it was decided that the statutory exemption would be replaced by a type exemption installed by the Controller which shall exempt various types of arrangements between air carriers, so as to prevent a sweeping and unwanted application of the binding arrangement section on the thousands of arrangements forming the basis of flight activity to and from Israel and which pose no threat to competitiveness.

As noted, on October 30 2008 the Ministry of Industry confirmed the type exemption set by the Controller. The type exemption deals with a broad variety of arrangements and exempts various operational arrangements, interline and cargo agreements not including minimal quota requirements for flight tickets or cargo loads and frequent flier agreements from detailed licensing requirements. The type exemption permits non-long-term "dry" lease agreements (leases of the aircraft only, sans crew) and "wet" lease agreements (leasing an aircraft and its crew), but sets special limitations on lease agreements made with Israeli air carriers. The exemption also applies to code share agreements, subject to broad restrictions and significant limitations set thereof. The type exemption includes

a transitional order, according to which a binding arrangement made prior to its coming into effect and which is covered by the statutory exemption shall not require approval until 9 months have passed since the beginning of the type exemption.

The type exemption is based on a previous draft published by the Controller several months ago regarding which the Company offered several remarks and reservations, which the Company submitted to the Controller in writing and orally. While the Controller included important and material amendments to the type exemption, in part as a result of the Company's remarks, the Company believes that the wording of the type exemption is still too restrained (particularly as regards the scope of the exemption given to code sharing agreements) and that it places unnecessarily burdensome regulatory restrictions which may harm the welfare of Israeli travelers as well as the Company's activities. The Company attends to submit a request to the Controller for amendments to the type exemption, in accordance with experience accumulated from the application of the type exemption in its present format. At the same time, the Company is preparing itself for the Amendment's coming into effect on January 1 2008, including by studying the need for approval from the Restraint of Trade Controller to carry out agreements involving the Company.

To item 9.11.10 – standardization

The IOSA (IATA Operational Safety Audit) for the Company has been completed and the Company has been informed that it has met all requirements for an IATA IOSA seal of approval, placing in the forefront of the world's airlines as regards aviation safety.

To item 9.11.12 – Security arrangements and to item 9.18.13 – Cost of maintaining aviation security

Pursuant to the update to the periodic report for the second quarter of 2008, on September 11 2008 the Government of Israel, the Minister of Finance, the Deputy Prime Minister and the Minister of Transportation and Road Safety submitted a preliminary response to the petition ("the State's Response"). According to the State's Response, on August 24 2008 the Government of Israel passed Resolution 4032 ("the Cancellation Resolution") which changes and limits the application of Government Resolution 3024 dated January 27 2008 ("the Original Resolution"), so that with the passing of the Cancellation Resolution, the basis of the petition underwent a material change and therefore the Court is requested to reject it (for details on the Cancellation Agreement see the update to item 7.1.10 above).

On September 18 2008 the Company filed a request to amend the petition ("the Petition Amendment Request"), this in light of the State's response, so that in the framework of the Amended Petition, the Company shall ask the Court to issue an order to the respondents, according to which they must provide cause as to why the Cancellation Resolution should not be revoked leaving the Original Resolution - the application of which has already begun - in effect, to be applied by the Government in full, and alternately, if the Cancellation Resolution is to remain in effect, why the situation should not be returned to its previous state prior to the original resolution, including the cancellation of the appointment of

other Israeli airlines as Designated Carriers, which was made as a result of the original resolution.

In accordance with the Court's decision dated September 21 2008, most of the respondents to the petition stated that they had no objection to the Petition Amendment Request. No ruling on the Petition Amendment Request has yet been made.

To item 9.14 – Legal proceedings

As reported by the Company on August 24 2008, the Korea Fair Trade Commission (hereinafter: "**the Korean Commission**") presented the Company with a request for information pertaining to an investigation the Korean Commission is holding regarding possible violations of Korean competitiveness rules in the field of air cargo shipping for the period starting 1999. To the best of the Company's knowledge, the Korean Commission is investigating a series of airlines. The Company responded as requested.

EL AL Israel Airlines Ltd.
Board of Directors' Report on the State of Corporate Affairs
For the period ended September 30, 2008

We hereby present the Board of Directors' report on the state of corporate affairs for the period ended September 30, 2008.

EL AL Israel Airlines Ltd. (hereinafter: "the Company") finished the 3 months ended September 30, 2008 with income of \$30.4 million, compared to income of \$40.7 million in the corresponding period last year.

It's worth noting that this result was achieved in the midst of a global crisis in the airline industry, which caused many airlines to curtail operations. Jet fuel prices increased by 67% in the third quarter of 2008, compared to the corresponding quarter last year, the NIS and euro were revaluated vs. the USD by an average rate of 17% and 9%, respectively, compared to the corresponding period in 2007, along with increasing competition from regular foreign airlines, which increased their seat supply at Ben Gurion Airport by 27% over the reported quarter compared to the corresponding period last year.

Company sales in the second quarter of this year increased by 7% over the corresponding period last year, reaching a record sum of \$607.3 million.

Gross income in the third quarter of 2008 amounted to \$133.4 million, 22% of turnover, whereas in the corresponding period last year, gross income amounted to \$151.8 million, 26.8% of turnover.

The balance of the Group's cash and short-term investments as of September 30, 2008 amounted to \$231.6 million.

Shareholders' equity as of September 30, 2008 amounted to \$266.6 million, compared to \$318.8 million as of December 31, 2007.

1. General

1.1 IFRS data update

In the first quarter of 2008, the Company started preparing its financial statements in accordance with International Financial Reporting Standards (IFRS). The transition date to international standards, as defined in Accounting Standard no. 29 by the Israeli Accounting Standards Board, was January 1, 2007. As a result of transition to IFRS-based reporting, the Company presented its financial statements for the reported period, as well as comparison figures for the 9-month and 3-month periods ended September 30, 2007 and for the year ended December 31, 2007 in accordance with international standards. The information presented in the Board of Directors' report and comparison figures are presented in accordance with international standards.

As for overall accounting implications and adjustments required due to transition from reporting based on Israeli GAAP to IFRS-based reporting, see Notes 1b and 9 to the Company's interim financial statements as of September 30, 2008.

1.2 The Company and its business environment

The Company acts as the State of Israel's designated air carrier for most international routes operating to and from Israel. The primary activity of the Company and its subsidiaries is the transport of passengers and cargo, including baggage and mail, by way of scheduled flights, as well as passenger transport via charter flights, between Israel and abroad. The Company also deals in the leasing of aircraft, in providing security services and general and comprehensive maintenance services at Ben Gurion Airport for aircraft

belonging to other airlines, in the sale of duty free items, and via investee companies - in ancillary activities, primarily the manufacture and supply of food to its planes and the management of a number of overseas travel agencies.

The business environment in which the Company operates is the civil, international and tourist aviation market to and from Israel, which is characterized by seasonality and a high level of competition, which grows fiercer at times of surplus capacity.

The Company has two operating segments:

- a. **Air transportation in passenger aircraft** - in this segment the Group transports passengers as well as cargo (including mail and baggage) in the belly of passenger aircraft, as well as provides ancillary services, such as sale of duty-free items and charter flights.
- b. **Air transport in cargo aircraft** - in this segment the Group transports cargo in cargo aircraft and provides ancillary services.

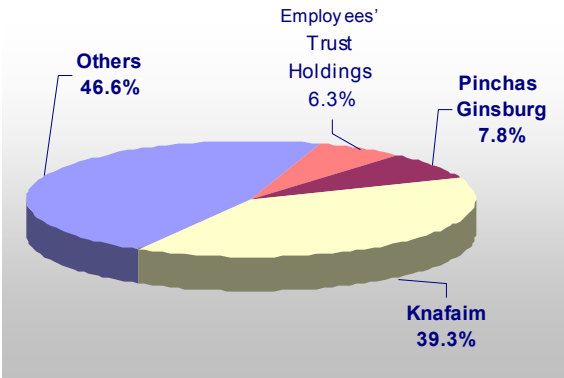
1.3 Holdings of Company shareholders

As of September 30, 2008, holdings in the Company are as follows:

Knafaim Holdings Ltd. ("Knafaim") - 39.3%; Pinchas Ginsburg - 7.7%; Employees' Trust Holdings - 6.3%; others - 46.6%.

For further details on the Company's privatization, see Note 1b of the December 31 2007 Periodic Report.

Ratio of Company Share Holdings
As of September 30, 2008 (Undiluted):



2. Financial data (consolidated reports)

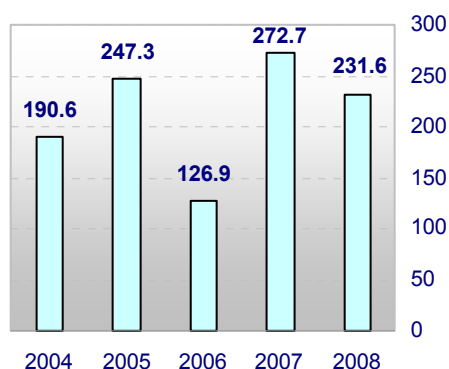
	30.09.2008	31.12.2007	change	
	in thousands US dollars	in thousands US dollars	in thousands US dollars	%
Assets				
Cash and cash equivalents & Short-term deposits	231,621	267,303	(35,682)	(13%)
Trade receivables	151,781	143,617	8,164	6%
Other receivables	38,300	22,254	16,046	72%
Derivative Financial instruments	29,939	25,530	4,409	17%
Prepaid expenses	25,958	25,096	862	3%
Inventories	17,446	15,981	1,465	9%
Long-term deposits	2,444	2,207	237	11%
Long-term investees	2,847	2,268	579	26%
Investments in another company	1,581	1,715	(134)	(8%)
Long-term derivative financial Instruments	11	7,570	(7,559)	(100%)
Fixed assets	1,282,454	1,285,752	(3,298)	(0%)
Other Intangible assets	7,111	4,388	2,723	62%
	1,791,493	1,803,681	(12,188)	(1%)
liabilities & Equity				
Short-term borrowings and current maturities	72,500	66,316	6,184	9%
Trade payables	179,296	167,420	11,876	7%
Other payables	46,462	47,185	(723)	(2%)
Provisions	100,265	89,621	10,644	12%
Proposed Dividend payable	-	3,008	(3,008)	
Current derivative financial instruments	21,239	-	21,239	
Current liability employee benefit obligations	87,012	87,578	(566)	(1%)
Deferred revenues	221,888	188,751	33,137	18%
Long-term loans from financial institutions	668,339	713,793	(45,454)	(6%)
Long-term employee benefit obligations	37,073	54,751	(17,678)	(32%)
Long-term loans from others	188	423	(235)	(56%)
Long-term derivative financial instruments	19,987	1,415	18,572	1313%
Long-term Provisions	16,684	-	16,684	
Deferred tax	53,967	64,576	(10,609)	(16%)
Shareholders' equity	266,593	318,844	(52,251)	(16%)
	1,791,493	1,803,681	(12,188)	(1%)

2.1 The primary changes in assets, liabilities and shareholders' equity as of September 30, 2008 compared to December 31, 2007 are as follows:

- Decrease in balance of cash, cash equivalents and short-term deposits amounting to \$35.7 million, primarily due to investments in fixed assets and other investments amounting to \$39.9 million, offset primarily from cash flow from ongoing activities to the amount of \$97.8 million.
- Increase in other accounts receivables, primarily due to a seasonal increase in passenger sales offset by a decrease in cargo sales.

- Increase in the accounts receivable balance deriving primarily from the increase in deposits placed by the Company at the disposal of the institutions hedging the jet fuel transactions and the increase in the debit balance of subsidiary Sun-Dor, as a result of the increase in its activity during summer months.
- The following changes occurred to the Company's derivative financial instruments:
 - The fair value of jet fuel hedging decreased by \$39.6 million as a result of the drop in jet fuel prices at the end of the third quarter. The fair value of interest hedging dropped by \$4.1 million as well compared to fair value at the end of 2007, as a result of the drop in LIBOR interest rates at the end of the period. The fair value of interest rate hedging increased by a sum of \$0.7 million, as a result of the NIS's revaluation vs. the USD in the first nine months of 2008. In total, a decrease of \$43.0 million in the fair value of the Company's financial instruments was noted in the reported period. The decrease in the fair value of derivative financial instruments, recognized as hedging agreements, was evident in the decrease in capital reserve in respect of cash flow hedges recognized directly in equity (some \$32.2 million before tax, some 23.8 million after tax), while the \$10.8 decrease in fair value of derivative financial instruments not recognized as cash flow hedges was charged as expenses in fuel and financing expense items. For further details, see Items 6.2, 6.3 and 6.4 of the Board of Directors' Report.
- The increase in other intangible assets is primarily due to payments on account of the new AMADEUS reservation system and the ERP system.
- Current maturities of long-term loans increased by \$6.8 million, while short-term credit decreased by \$0.6 million.
- An increase in Trade payables deriving primarily from the increase in the balances of engine repair suppliers balance following several repairs occurring towards the end of the third quarter of 2008, the payment date of which falls on the next quarter.
- Increase in current and long term accruals, primarily due to an accrual made by the Company in the first quarter of 2008, amounting to \$20 million with regard to an inquiry by the Antitrust Division of the US Department of Justice into the air cargo sector – see Note 5b1 to the interim financial statements as of September 30, 2008.
- Decrease in dividend proposed for payment is due to dividend payment in January 2008.
- Increase in prepaid expenses, primarily due to prepaid commissions due to an increase in passenger sales.
- The balance of long term loans (including current maturities) decreased due to regular repayment of loans.
- Decrease in long term liabilities regarding employee benefits, primarily due to a decrease in liability for early retirement programs due to regular payments and deposits for 2009.
- Decrease in net deferred income tax liabilities, is primarily due to decrease in fair value of financial transactions designated as hedges, as well as from deferred tax revenues recorded by the Company in the reported period due to the loss for the period.
- Decrease in Company shareholders' equity, primarily due to loss accumulated for the period and the decrease in capital reserve in respect of cash flow hedges recognized directly in equity.

**Cash and cash equivalents and
short-term deposits
as of September 30
(in millions of dollars)**



As of Sept 30, 2008, the Company has a working capital deficit amounting to \$233.6 million, compared to a working capital deficit of \$150.1 as of December 31, 2007. The Company's current ratio as of September 30, 2008 is 67.9%, compared to 76.9% as of December 31, 2007. The increase in working capital deficit is primarily due to the decrease in cash balances and short term deposits, the increase in unearned revenues due to the increase in sale of flight tickets not yet utilized as well as the increase in suppliers and the fair value decrease in derivative financial instruments.

The working capital deficit arises from the Company's current liabilities, which include two major components: unearned revenues from sale of flight tickets as well as current maturities of long-term loans. These components, typical of current business cycles, are included under current liabilities and explain most of the working capital deficit.

3. Analysis of EL AL operating business results

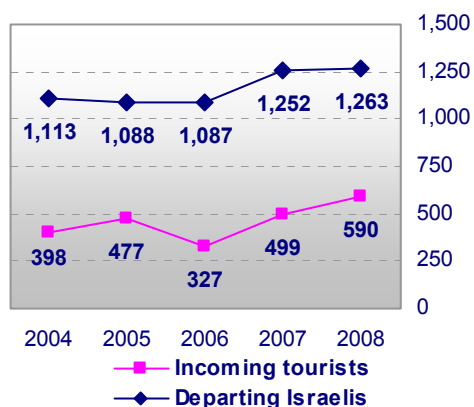
3.1 Market data

Passenger and cargo traffic at BGA	Jul - Sep 2008	Jul - Sep 2007	change	
	in thousands	in thousands	in thousands	%
Incoming tourists *	590	499	91	18%
Departing Israelis *	1,263	1,252	11	1%
Cargo import - tons **	35	35	0	0%
Cargo export - tons **	39	42	(3)	(8%)
Passenger and cargo traffic at BGA	Jan - Sep 2008	Jan - Sep 2007	change	
	in thousands	in thousands	in thousands	%
Incoming tourists *	1,655	1,318	337	26%
Departing Israelis *	2,824	2,732	92	3%
Cargo import - tons **	109	102	7	7%
Cargo export - tons **	142	143	(1)	(1%)

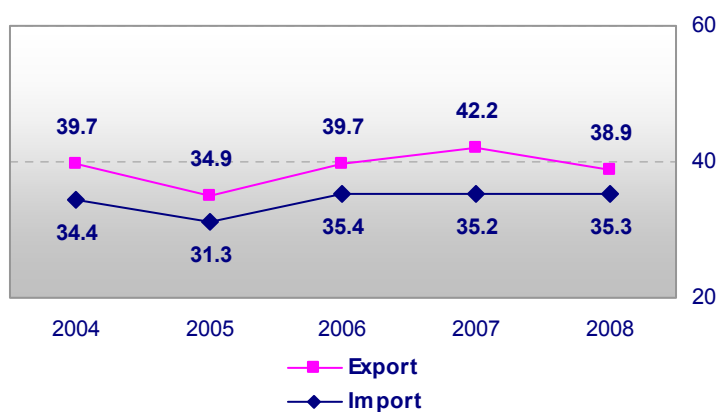
* Source: Central Bureau of Statistics.

** Excluding cargo in transit.

Incoming tourists and departing Israelis, in the third quarter of the years (in thousands):



Import and export of cargo by air to and from Israel, in the third quarter of the years (in thousands):



3.2 Company Operating Data

	Jul - Sep 2008	Jul - Sep 2007	change
Passenger leg (scheduled and chartered) - in thousands	1,137	1,149	(1%)
scheduled) - in millions) RPK	4,558	4,953	(8%)
scheduled) - in millions) ASK	5,335	5,691	(6%)
Load factor (scheduled)	85.4%	87.0%	(2%)
The Company's market share (scheduled and chartered)	32.6%	35.3%	(7%)
Flown cargo, in thousand tons	24	36	(34%)
in millions - RTK	126,803	213,809	(41%)
Weighted flying hours (including leased equipment) - in thousands (*)	42.1	47.8	(12%)
Average man-years (EI AL only):			
Permanent	3,780	3,544	7%
Temporary	2,406	2,660	(10%)
Total	6,186	6,204	(0.3%)

	Jan - Sep 2008	Jan - Sep 2007	change
Passenger leg (scheduled and chartered) - in thousands	2,981	2,828	5%
scheduled) - in millions) RPK	12,907	12,833	1%
scheduled) - in millions) ASK	15,660	15,008	4%
Load factor (scheduled)	82.4%	85.5%	(4%)
The Company's market share (scheduled and chartered)	35.6%	37.5%	(5%)
Flown cargo, in thousand tons	88	111	(21%)
in millions - RTK	468	612	(24%)
Weighted flying hours (including leased equipment) - in thousands (*)	126.3	127.2	(1%)
<u>Average man-years (EI AL only):</u>	0	0	0
Permanent	3,754	3,546	6%
Temporary	2,366	2,394	(1%)
Total	6,120	5,940	3%
Aircraft in operation - end of period - number of units	35	37	(2)
Average age of owned fleet at the end of the period - in years	14.7	14.5	0.2

Legend:

Passenger leg – one-way flight voucher.

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

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

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

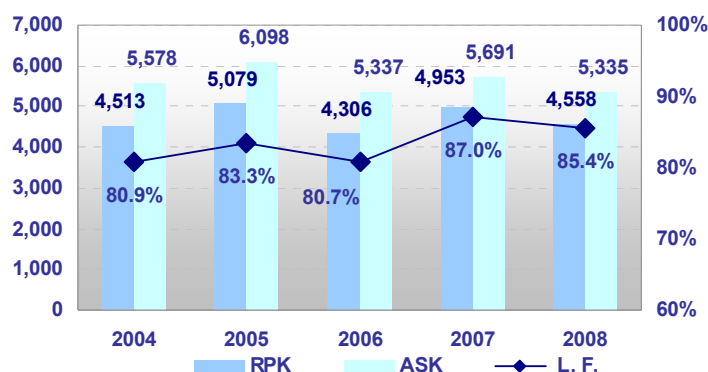
Passenger Load Factor (passenger occupancy) – revenue passenger kilometers as percentage of available seat kilometers.

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

Aircraft weightings: Boeing 757/767 = 1.0; Boeing 747 = 2.0; Boeing 777 = 1.6; Boeing 737 = 0.6.

These weightings have been determined based on estimated total expenses by aircraft type, and are consistently used to calculate weighted flight hours as an indicator of extent of flight operations.

**Operational benchmarks, in the third quarter:
(in millions)**



3.3 Profit and Loss Data

For the three-month period ended September 30, 2008 (consolidated reports):

	<u>Jul - Sep</u> 2008		<u>Jul - Sep</u> 2007		<u>change</u>	
	in thousands US dollars	% of operating revenues	in thousands US dollars	% of operating revenues	in thousands US dollars	%
Revenues Operating	607,273	100%	566,715	100%	40,558	7%
Operating expenses	473,865	78.0%	414,877	73.2%	58,988	14%
Gross profit	133,408	22.0%	151,838	26.8%	(18,430)	(12%)
Selling expenses	63,865	10.5%	65,967	11.6%	(2,102)	(3%)
General and administrative expenses	24,560	4.0%	21,675	3.8%	2,885	13%
Other operating expenses (revenues),net	(5,412)	(0.9%)	2,445	0.4%	(7,857)	
Operating loss before financing	50,395	8.3%	61,751	10.9%	(11,356)	(18%)
Financing expenses	(12,029)	(2.0%)	(15,842)	(2.8%)	3,813	(24%)
Financing income	1,986	0.3%	4,504	0.8%	(2,518)	(56%)
Loss before income taxes	40,352	6.6%	50,413	8.9%	(10,061)	(20%)
Income taxes	(10,402)	(1.7%)	(9,720)	(1.7%)	(682)	7%
Loss after taxes	29,950	4.9%	40,693	7.2%	(10,743)	(26%)
Company's equity in results of affiliates, net	480	0.1%	54	0.0%	426	789%
Profit for the period	30,430	5.0%	40,747	7.2%	(10,317)	(25%)

The primary factors influencing the business results for the three month period ending September 30 2008, compared to the same period last year are:

- The increase in operating revenues is primarily due to the increase in passenger revenues due to average revenue per passenger-kilometer. Cargo aircraft revenues decreased from some \$50 million in the third quarter of 2007 to some \$29 million in the reported period due to discontinuation of cargo aircraft operations to East Asia in the reported period. Other revenues also increased, primarily due to the sale of duty-free items and the provision of maintenance services to external entities.
- In the third quarter of 2008, the Company's operating expenses increased over the corresponding period last year, primarily due to an increase in salary expenses and jet fuel expenses, as detailed below.
- Salary expenses in the third quarter of 2008 increased, primarily due to revaluation of the NIS vs. the USD by an average of 17% over the same period last year – which led to increase in NIS-denominated salary expenses in USD terms. For impact of changes in NIS/USD exchange rates on Company liabilities, see section 3.4 below.
- Company jet fuel expenses increased from \$153.5 million in the third quarter of 2007 to \$214.7 million in the reported quarter – a 40% increase. This is after hedging reimbursement of \$13.7 million in the third quarter of 2008 (compared to hedging reimbursement amounting to \$5.1 million in the same period last year). The fair value of jet fuel hedging not classified as hedging agreements in the reported period decreased by \$3.8 million (compared to a \$0.9 million increase in fair value in the corresponding period last year).

The increase in fuel expenses is primarily due to a 67% increase in effective jet fuel price

for the Company, offset by a decrease in expenses, as a result of a decrease in flight hours in the reported period compared to the corresponding quarter last year.

In the third quarter of 2008, fuel expenses accounted for 35.4% of Company turnover, compared to 27.1% in the corresponding period last year.

For hedging of jet fuel prices, see section 6.2 below.

- Selling expenses decrease compared to the corresponding period last year, primarily due to decreases in the rate of distribution, offset by the increase in salary expenses mentioned above.
- General and administrative expenses increased, primarily due to an increase in salary expenses due to the revaluation of the NIS vs. the USD and the increase in legal expenses, chiefly due to the investigations in the field of air cargo shipping services.
- In the reported period, the Company recorded other net expenses amounting to \$5.4 million, primarily due to capital gains resulting from the sale of a Boeing 767 aircraft. The Company listed \$2.4 million in additional expenses in the third quarter of 2007, primarily due to early retirement programs.
- The decrease in financing expenses in the second quarter of 2008 compared to the same period last year is primarily due to decrease in interest expenses for the Company's loans due to a decline in LIBOR interest rates and from a decrease in exchange rate differential expenses due to revaluation of the USD vs. the NIS and euro in the reported period, offset by an increase in exchange rate and interest rate hedging expenses, primarily by the decrease in the fair value of these transactions in the reported period.
- Financing income for the Company decreased, primarily due to a decrease in income from interest on deposits as a result of dropping LIBOR rates and the decrease in deposits in the reported period compared to the corresponding period last year and the decrease in fair value of exchange rate and interest hedging transactions. For hedging of exchange rates and interest rates, see sections 6.3 and 6.4 below.

Profit and loss data

For the nine-month period ended September 30, 2008 (consolidated reports):

	<u>Jan - Sep</u> 2008		<u>Jan - Sep</u> 2007		<u>change</u>	
	in thousands US dollars	% of operating revenues	in thousands US dollars	% of operating revenues	in thousands US dollars	%
Revenues Operating	1,635,761	100%	1,408,156	100%	227,605	16%
Operating expenses	1,373,844	84.0%	1,096,447	77.9%	277,397	25%
Gross profit	261,917	16.0%	311,709	22.1%	(49,792)	(16%)
Selling expenses	180,434	11.0%	159,552	11.3%	20,882	13%
General and administrative expenses	75,647	4.6%	66,707	4.7%	8,940	13%
Other operating expenses (revenues), net	18,702	1.1%	(4,174)	(0.3%)	22,876	
Operating profit (loss) before financing	(12,866)	(0.8%)	89,624	6.4%	(102,490)	
Financing expenses	(37,964)	(2.3%)	(37,578)	(2.7%)	(386)	1%
Financing income	18,313	1.1%	11,068	0.8%	7,245	65%
Profit (loss) before income taxes	(32,517)	(2.0%)	63,114	4.5%	(95,631)	
Income taxes	2,530	0.2%	(13,135)	(0.9%)	15,665	
Profit (loss) after taxes	(29,987)	(1.8%)	49,979	3.5%	(79,966)	
Company's equity in results of affiliates, net	578	0.0%	145	0.0%	433	299%
Profit (loss) for the period	(29,409)	(1.8%)	50,124	3.6%	(79,533)	

The primary factors influencing the business results for the nine month period ending September 30 2008, compared to the same period last year are:

- Increase in operating revenues is primarily due to increase in passenger revenues due to higher number of passengers flown and higher average revenue per passenger-kilometer. Income from cargo aircraft decreased from some \$147 million in the first nine months of 2007 to \$114 million in the reported period, among other reasons from the discontinuation of cargo service to East Asia starting in the second quarter of 2008. Other revenues also increased, primarily due to the sale of duty-free items and the provision of maintenance services to external entities.
- In the first nine months of 2008, operating expenses for the Company increased over the same period last year, primarily due to salary expenses and rising fuel prices, as detailed below, and the devaluation of the USD vs. the NIS and Euro.
- The increase in the Company's salary expenses derived primarily from the devaluation of the USD vs. the NIS and euro, which increase NIS salary expenses in USD terms, as well as from the increase in average number of employee as a result of increased activity.

In the matter of the influence of the changes in USD vs. NIS rates of exchange on the Company's provisions, see Item 3.4 below.

- The increase in jet fuel expenses from \$374.1 million in the first nine months of 2007 to \$593.1 million in the reported period, a 59% increase. This after receiving hedging refunds to the amount of \$42.0 million (compared to a hedging refund of \$1.7 million for the corresponding period last year). The fair value of jet fuel hedging transactions not classified as defense agreements decreased by \$9.7 million (compared to a fair value increase of \$15.1 million in the corresponding period last year).

The above increase in fuel expenses derives primarily from a 66% increase in the Company's effective jet fuel prices compared to the corresponding period last year. In the first 9 months of 2008, fuel expenses accounted for 36.3% of the Company's turnover compared to 26.6% in the corresponding period last year. As regards the hedging of jet fuel prices, see Item 6.2 below.

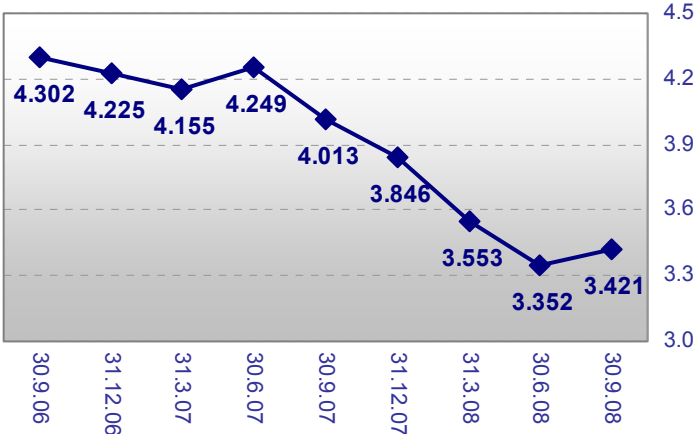
- Selling expenses in the first nine months of 2008 increased, primarily due to an increase in salary expenses due to USD devaluation an increase in distribution expenses due to expanded operations, this despite the fact that their share of the turnover has decreased, as well as an increase in advertising expenses.
- General and administrative expenses increased in the first nine months of 2008 compared to the corresponding period last year, primarily due to increase in salary expenses as mentioned above, and from the revaluation of the NIS vs. the USD at an average rate of 17%. However, their percentage out of total turnover in the reported period remained unchanged from the same period last year.
- In the reported period, the Company recorded other net expenses amounting to \$18.7 million, compared to other net revenues amounting to \$4.2 million in the first 9 months of 2007. Most of the expenses in the reported period are due to a provision made by the Company in the first quarter of 2008, amounting to \$20 million due to an inquiry by the Antitrust Division of the US Department of Justice into air cargo transportation services; other expenses were recorded due to revaluation of the NIS vs. the USD - which increased Company liabilities in respect of early retirement programs. On the other hand, a capital gain of \$4.7 million was listed from the sale of a 767 aircraft in the third quarter of 2008. In the first nine months of 2007 the Company recorded revenues due to reimbursement received from Boeing Corp. and from vacating a leased property at Heathrow Airport, offset by a provision for an early retirement program.
- Financing expenses remained largely unchanged. On the one hand, exchange rate differential expenses deriving from the devaluation of the USD vs. other currencies increased, while interest expenses on loans decreased due to decreases in LIBOR interest rates.
- Financing revenues of the Company increased, primarily due to increase in fair value of exchange rate hedging transactions executed by the Company, offset by a decrease in income from interest on deposits as a result of the decrease in LIBOR rates.
- In the first nine months of 2008, a tax benefit was recorded amounting to \$2.5 million - compared to tax expenses amounting to \$13.1 million in the first nine months of 2007 - due to pre-tax loss in the reported period compared to pre-tax income in the same period last year.

3.4 Impact of exchange rate changes on Company liabilities in respect of employee benefits

In the 3-month period ended September 30, 2008, the NIS was devaluated against the USD by 2.1%, compared to a revaluation of 5.6% in the corresponding period last year.

In the first nine months of 2008, the NIS was revaluated against the USD by 11.1%, compared to a revaluation of 5.0% in the corresponding period last year.

Changes in US Dollar exchange rate – NIS per day:



The Company has net liabilities in respect of employee benefits, primarily retirement programs, sick pay and paid leave payout, amounting to \$83 million as of September 30, 2008.

Since most of these liabilities are NIS-denominated, whereas the Company's functional currency is USD, these liabilities should be translated into USD, which causes differentials due to changes in the NIS/USD exchange rate. Changes in exchange rates are not uni-directional, and cause revenues or expenses to be recorded in the Company's financial statements. These revenues or expenses do not impact cash flow or operating costs of the Company in the short-term. In order to compare business results of the Company over time, these revenues or expenses should be excluded.

In the quarter ended September 30, 2008, expenses for this item decreased by \$1.5 million, compared to the corresponding period last year, when expenses were recorded for this item at by \$4.4 million.

In the first nine months of 2008, expenses were recorded for this item amounting to \$9.0 million, compared to the corresponding period last year, when expenses for this item were recorded amounting to \$5.3 million.

The following details the Company's business results, neutralized from the influence of the exchange rate on the liability component due to employee-employer relations, as described above:

Three-month period ended september 30,	<u>Before</u>		<u>After</u>	
	<u>neutralizing the exchange-rate effect</u>			
	<u>on the accrued severance pay</u>			
	2008	2007	2008	2007
	(in thousands US dollars)			
Operating expenses	473,865	414,877	474,606	412,872
Gross profit	133,408	151,838	132,667	153,843
Gross profit rate	22.0%	26.8%	21.8%	27.1%
Selling, general and administrative expenses	88,425	87,642	88,519	87,383
Other operating expenses (income),net	5,412	(2,445)	4,713	(277)
Operating loss before financing expenses	50,395	61,751	48,861	66,183
Operating loss rate before financing	8.3%	10.9%	8.0%	11.7%
Net loss for the period	30,430	40,747	28,896	45,179
Net loss for the period rate	5.0%	7.2%	4.8%	8.0%

Nine-month period ended september 30,	<u>Before</u>		<u>After</u>	
	<u>neutralizing the exchange-rate effect</u>			
	<u>on the accrued severance pay</u>			
	2008	2007	2008	2007
	(in thousands US dollars)			
Operating expenses	1,373,844	1,096,447	1,369,939	1,093,654
Gross profit	261,917	311,709	265,822	314,502
Gross profit rate	16.0%	22.1%	16.3%	22.3%
Selling, general and administrative expenses	256,081	226,259	255,589	225,783
Other operating expenses (income),net	(18,702)	4,174	(14,147)	6,160
Operating profit (loss) before financing expenses	(12,866)	89,624	(3,914)	94,879
Operating profit (loss) rate before financing	(0.8%)	6.4%	(0.2%)	6.7%
Net profit (loss) for the period	(29,409)	50,124	(20,457)	55,379
Net profit (loss) for the period rate	(1.8%)	3.6%	(1.3%)	3.9%

3.5 Segment reporting

Below is information by geographic segment, on consolidated basis:

Three-month period ended:					
	North America	Europe	Central Asia Far & East	Rest of the world	Total
30.09.2008 -(unaudited)	(in millions US dollars)				
operating revenues *	207.1	305.0	69.8	11.6	593.5
Non-segment revenues					13.8
Total consolidated revenues					607.3
Operating income **	14.7	64.7	9.2	1.8	90.4
Overall segment expenses, net					(40.0)
Operating income, before financing expenses - consolidated					50.4
% of operating revenues	7.1%	21.2%	13.2%	15.2%	
30.09.2007 -(unaudited)	(in millions US dollars)				
operating revenues *	204.7	256.7	85.5	11.1	558.0
Non-segment revenues					8.7
Total consolidated revenues					566.7
Operating income **	27.6	64.8	8.6	4.0	105.0
Overall segment expenses, net					(43.2)
Operating income, before financing expenses - consolidated					61.8
% of operating revenues	13.5%	25.2%	10.1%	36.4%	

Nine-month period ended:					
	North America	Europe	Central Asia Far & East	Rest of the world	Total
30.09.2008 -(unaudited)	(in millions US dollars)				
operating revenues *	562.4	773.1	232.2	36.8	1,604.5
Non-segment revenues					31.2
Total consolidated revenues					1,635.8
Operating income **	11.8	109.8	22.4	5.5	149.5
Overall segment expenses, net					(162.4)
Operating income (loss), before financing expenses - consolidated					(12.9)
% of operating revenues	2.1%	14.2%	9.7%	14.8%	
30.09.2007 -(unaudited)	(in millions US dollars)				
operating revenues *	501.0	611.8	240.5	30.1	1,383.4
Non-segment revenues					24.8

Total consolidated revenues					1,408.2
Operating income **	44.9	121.5	19.6	9.9	195.8
Overall segment expenses, net					(106.2)
Operating income, before financing expenses - consolidated					89.6
% of operating revenues	9.0%	19.9%	8.2%	32.9%	

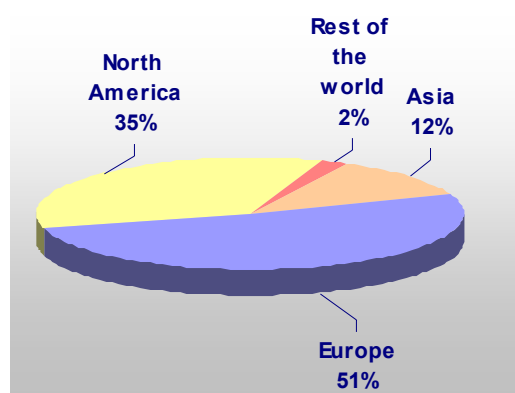
For year ended:					
	North America	Europe	Central Asia Far & East	Rest of the world	Total
31.12.2007 -(audited)	(in millions US dollars)				
operating revenues *	674.7	822.3	356.8	42.1	1,895.9
Non-segment revenues					36.5
Total consolidated revenues					1,932.5
Operating income **	56.7	144.1	33.4	11.2	245.4
Overall segment expenses, net					(150.7)
Operating income, before financing expenses – consolidated					94.7
% of operating revenues	8.4%	17.5%	9.4%	26.7%	

* Income is attributed to geographical sectors by flight destination.

In the reported period and in the nine month period ending September 30 2008, revenues increased in the all sectors over the corresponding period last year, with the exception of Central Asia and East Asia, while operating income in all segments with the exception of Central Asia and East Asia decreased compared to the corresponding periods in 2007. The decrease in operating income in North America, Europe and the Rest of the World is primarily due to the increase in operating expenses, as set forth in section 3.3 of the Board of Directors' report above.

In the Central Asia and East Asia sector revenues decreased, but operating income increased, primarily due to discontinuation of cargo aircraft operations to East Asia destinations, which are heavy on fuel consumption and imbalanced in terms of cargo traffic volume.

Note that the increase in un-attributed cross-segment expenses, from \$106 million in the first nine months of 2007 to \$162 million in the first nine months of 2008, is primarily due to other expenses amounting to \$18.7 million (primarily due to a provision made by the Company in respect of an inquiry into cargo air transport services, amounting to \$20 million) in the reported period, compared to other revenues amounting to \$4.2 million generated by the Company in the same period last year, due to increase in payroll expenses not attributed to sectors, as set forth in section 3.3 of the Board of Directors' report, and to higher prices for fixed un-attributed expenses.

Breakdown of revenues attributed to geographic sectors**JUL-SEP 2008:****4. Seasonality**

Passenger traffic at Ben Gurion airport is highly seasonal. Most of the activity is in the summer months, with the peak being in July-September. Winter months (January-March) see low volume of passenger traffic, but higher cargo shipping of agricultural produce to Europe in that period.

5. Liquidity and Sources of Financing

Cash flow movements in the 9-month and 3-month periods ended September 30, 2008 compared to the corresponding periods last year are:

	Jul - Sep 2008 in thousands US dollars	Jul - Sep 2007 in thousands US dollars	change in thousands US dollars
Cash flows from operating activities	(11,348)	74,083	(85,431)
Cash flows used for investing activities	42,685	(294,422)	337,107
Cash flows used for financing activities	(18,378)	150,535	(168,913)
Net increase (decrease) in cash	12,959	(69,804)	82,763

	Jan - Sep 2008 in thousands US dollars	Jan - Sep 2007 in thousands US dollars	change in thousands US dollars
Cash flows from operating activities	97,849	178,081	(80,232)
Cash flows used for investing activities	(38,438)	(396,535)	358,097
Cash flows used for financing activities	(43,573)	161,439	(205,012)
Net increase (decrease) in cash	15,838	(57,015)	72,853

In the quarter ended September 30, 2008, the Company used a cash flow from operating activities amounting to \$11.3 million (compared to a cash flow of \$74.1 million in the corresponding period last year.) This change derives primarily from a decrease in suppliers, payables, and unearned income caused, among other reasons, from the drop in jet fuel prices, from the decrease in pre-tax revenue for the reported period compared to the pre-tax revenue for the corresponding period last year, from the devaluation of the NIS vs. the USD which decreased NIS supplier and payable balances, in USD terms, as

well as a seasonal decrease in revenue from the sale of flight tickets not yet utilized.

In the third quarter of 2008, the Company derived \$42.7 million from investing activities (compared to \$294.4 million used in the same period last year), primarily due to the net redemption of short-term deposits of \$66.6 million (compared to a net investment in short term deposits of \$110.4 million in the same period last year), from the return from the sale of fixed assets to the amount of \$6.5 million, offset by investments in fixed and intangible assets of \$30.5 million (of which \$4.8 million was on account of new aircraft acquisition), compared to investments in fixed and intangible assets of \$184.1 million for the corresponding period last year million (of which \$159.1 million was on account of new aircraft acquisition)

In the third quarter of 2008, the Company used \$18.4 million for financing activities, primarily repayment of long-term loans amounting to \$17.3 million (compared to \$150.5 million derived from financing activities in the same quarter last year, primarily from loans for the purchase of aircraft to the amount of \$219.4 million from bank institutions and \$61.3 million in the repayment of long term loans).

In the first nine months of 2008, the Company generated cash from operating activities amounting to \$97.8 million (compared to \$178.1 million in the same period last year).

The drop in cash flow from operating activities in the first nine months of 2008, over the same period last year, is primarily due to the pre-tax periodic loss in the first nine months of 2008 compared to the pre-tax periodic profit in the first nine months of 2007.

In the nine month period ending September 30 2008, the Company used \$38.4 million in investing activities, primarily for investments in fixed and intangible assets to the amount of \$97.0 million (of which \$34 million was on new aircraft), offset by net repayment of deposits to the amount of \$51.5 million (compared to \$396.5 million used in the same period last year, primarily for the purchase of aircraft and fixed and intangible assets totaling \$221.7 million and to investment in net short-term deposits of \$178.9 million. In addition, the Company received the proceeds from the sale of fixed assets, primarily from the sale of an aircraft, totaling \$7.0 million (compared to proceeds from the sale of fixed assets totaling \$0.4 million in the corresponding period last year).

In the nine month period ending September 30 2008, the Company used \$43.6 million for financing activities, primarily repayment of long-term loans amounting to \$39.9 million and dividend payment amounting to \$3.1 million (compared to \$161.4 million generated by the Company from financing operations in the corresponding period last year, primarily from long term loans from financial institutions for the purchase of aircraft to the amount of \$219.4 million and the exercise of option warrants into shares amounting to \$31.8 million, offset by repayment of long-term loans amounting to \$81.4 million).

Cash and cash equivalents and short-term investments as of September 30, 2008 amounted to \$231.6 million, compared to \$267.3 million as of December 31, 2007 (as of September 30, 2007 - \$272.7 million).

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

6.1 The Company's Policy Regarding the Management of Market Risks, Those Responsible for their Management, Means of Supervision and Policy Realization

The Company has a Board of Directors Committee for the purpose of managing market risks led by the Chairman of the Finance, Budget and Balance Sheet Committee, Mr. Nadav Palti, which is responsible for determining the Company's policy for covering existing exposure. The CFO is responsible for executing the policy and reporting to the Market Risk Management Committee.

The Market Risk Management Committee sets the future jet fuel consumption frameworks to be covered via financial hedging. In addition, from time to time the Committee examines the need to invest in derivatives, to diminish the exposure from interest risks and currency risks.

Over the course of the account period, the Company continued to implement corporate policy as regards market risk management and supervisory measures, as described in the Report of the Board of Directors on the State of the Corporation's Affairs dated December 31 2007 and in the Notes to the Financial Statements of that date.

Between January 1 2008 and the publishing of this Report, the Company held regular meetings of the Risk Management Committee, a Board of Directors subcommittee. In these meetings the Company management discussed the Company's status in the matter of exposure related to fuel, interest rates and rates of exchange.

A decision was reached as part of said discussions not to deviate from existing policy

For details on the policy implemented, see Items 6.2, 6.3 and 6.4 below.

For details of impact subsequent to the balance sheet date, see section 11b below.

For the Company's accounting policy as regards hedging, see Note 1n of the Company's September 30 2008 Interim Financial Statements.

6.2 Hedging of jet fuel prices

The Company, from time to time, conducts hedging transactions for jet fuel prices in accordance with its policy as put forth in Item 6.1 above. Some of these transactions are recognized as accounting hedging transactions, and some are not. The fair value of the jet fuel hedging transactions as of September 30 2007 is a net negative sum of \$10.1 million, presented in the financial statements in the framework of liabilities and assets in item: "Derivative Financial Instruments." For details regarding changes occurring after the balance sheet date, see Item 11b. below.

6.3 Hedging of loan interest rates

The Company enters into transactions with banks in Israel in order to hedge exposure in its long-term credit portfolio due to interest rate changes. No further transactions took place in the reported period.

In accounting terms, some of the aforementioned financial instruments were not designated as hedging transactions, while others were so designated.

After the aforementioned hedges, as of September 30, 2008, some 54% of the Company's outstanding loan balance bears fixed interest. The percentage of Company loans bearing fixed interest is gradually decreasing, for a term of up to 4 years.

The fair value of interest hedging instruments as of September 30, 2008 is a net negative amount of \$5.5 million, which is primarily presented in the financial statements under the non-current liabilities item "Derivative Financial Instruments".

For further information with regard to these transactions, see Item 11c below.

6.4 Hedging of exchange rates

In 2007, the Company entered into multiple financial transactions aimed at hedging against decrease in USD/NIS exchange rates in 2008. These transactions are not designated, in accounting terms, as hedging transactions.

The fair value of these instruments as of September 30, 2008 is \$4.4 million, presented in the financial statements under the current assets item "Derivative Financial Instruments".

For details of impact subsequent to the balance sheet date, see section 11d below.

6.5 Reporting of sensitivity analysis

Below is a sensitivity analysis of the fair value of financial instruments sensitive to potential changes in the risk factors to which they are exposed. This sensitivity analysis was prepared relative to the fair value of said financial instruments as of September 30, 2008.

Below are tables for sensitivity tests of instruments sensitive to changes in market prices:

a. Sensitivity to change in USD/NIS exchange rate - in thousands of dollars:

	Gain (loss) from changes		Fair value	Gain (loss) from changes	
	Increase 10% 3.763 NIS/\$	Increase 5% 3.592 NIS/\$		Decrease 5% 3.250 NIS/\$	Decrease 10% 3.079 NIS/\$
Cash and cash equivalents	(178)	(93)	1,963	103	218
Short-term investments	(783)	(410)	8,613	453	957
Trade accounts receivable	(40)	(21)	439	23	49
Receivables and other current assets	(726)	(380)	7,984	420	887
Current derivative financial instruments	(398)	(209)	4,381	231	487
Long-term bank deposits	(222)	(116)	2,444	129	272
Total financial Assets	(2,348)	(1,230)	25,824	1,359	2,869
Short-term bank borrowings	12	6	(128)	(7)	(14)
Trade accounts payable	2,682	1,405	(29,506)	(1,553)	(3,278)
Payables and other current liabilities	550	288	(6,049)	(318)	(672)
accruals	4,653	2,437	(51,179)	(2,694)	(5,687)
Current liability for employee benefits	7,599	3,981	(83,591)	(4,400)	(9,288)
Total financial liabilities	15,496	8,117	(170,453)	(8,971)	(18,939)
Exposure in linkage balance sheet due to surplus financial liabilities over financial assets *	13,148	6,887	(144,629)	(7,612)	(16,070)

* Excluding exposure due to impact of changes in exchange rates on liabilities in respect of long-term employee benefits, as set forth in section 3.4.

b. Sensitivity to change in USD/Euro exchange rate - in thousands of dollars:

	Gain (loss) from changes		Fair value 0.684 Euro/\$	Gain (loss) from changes	
	Increase 10% 0.753 Euro/\$	Increase 5% 0.718 Euro/\$		Decrease 5% 0.650 Euro/\$	Decrease 10% 0.616 Euro/\$
Cash and cash equivalents	(400)	(210)	4,402	232	489
Trade accounts receivable	(1,301)	(682)	14,316	753	1,591
Receivables and other current assets	(96)	(50)	1,055	56	117
Total financial Assets	(1,798)	(942)	19,773	1,041	2,197
Short-term bank borrowings	16	8	(174)	(9)	(19)
Trade accounts payable	2,814	1,474	(30,952)	(1,629)	(3,439)
Payables and other current liabilities	304	159	(3,342)	(176)	(371)
Current liability for employee benefits	51	27	(563)	(30)	(63)
Total financial liabilities	3,185	1,668	(35,031)	(1,844)	(3,892)
Exposure in linkage balance sheet due to surplus financial liabilities over financial assets*	1,387	727	(15,258)	(803)	(1,695)

* Excluding exposure due to impact of changes in exchange rates on liabilities in respect of long-term employee benefits, as set forth in section 3.4.

c. Sensitivity of jet fuel hedges to changes in jet fuel prices - in thousands of dollars:

In accordance with model principles, jet fuel hedging instruments have been grouped by similar reaction to market factors, since no material information, required for understanding the Company's exposure to market risk, is lost due to such grouping.

Type of instrument	Gain from changes		Fair value **	Loss from changes	
	Increase 10% 3.124 \$/gallon	Increase 5% 2.982 \$/gallon		Decrease 5% 2.698 \$/gallon	Decrease 10% 2.556 \$/gallon
Options - not designated for defense	2,131	1,194	8,886	(1,518)	(3,430)
SWAP transactions - designated for defense	35,541	17,771	(19,023)	(17,771)	(35,541)
Total fuel transactions	37,672	18,965	(10,137)	(19,289)	(38,971)

* Most of the gain or loss from changes to fair value is to be recognized directly in equity, rather than in the income statement.

** The price of jet fuel in the Mediterranean region as of September 30, 2008, used to calculate the fair value of the Company's jet fuel hedging transactions.

d. Sensitivity of interest hedges to changes in market interest rates - in thousands of dollars:

In accordance with model principles, interest rate hedging instruments have been grouped by similar reaction to market factors (SWAP transactions with Knock-Out not designated as hedges, IRS transactions designated as hedges, IRS transactions not designated as hedges), since no material information, required for understanding the Company's exposure to market risk, is lost due to such grouping

Type of instrument	Gain (Loss) from changes		Fair value *	Gain (Loss) from changes	
	Increase 10% in interest rate	Increase 5% in interest rate		Decrease 5% in interest rate	Decrease 10% in interest rate
SWAP transactions with KNOCK OUT- not designated for defense	(182)	(389)	672	(891)	(1,162)
IRS transactions- designated for defense	2,986	2,414	(1,734)	1,269	697
IRS transactions - not designated for defense	6,335	4,649	(2,966)	1,282	(404)
Cylinder transactions - not designated for defense	2,165	1,822	(1,492)	1,151	820
Total	11,304	8,496	(5,520)	2,811	(49)

* Fair value calculated according to LIBOR market interest rates as of the balance sheet date, as follows: 3-month LIBOR: 4.05%, 6-month LIBOR: 3.98% and 12-month LIBOR - 3.96% - as the case may be and as per specific transactions.

** The change in fair value of such instruments designated as hedges will be recognized directly in equity, rather than in the income statement.

e. Sensitivity of USD/NIS exchange rate hedge to change in market exchange rates - in thousands of dollars:

Type of instrument	Loss from changes		Fair value NIS/\$	Gain from changes	
	Increase 10% in exchange rate	Increase 5% in exchange rate		Decrease 5% in exchange rate	Decrease 10% in exchange rate
	3.763	3.592	3.421	3.250	3.079
Cylinder transactions- not designated for defense	(2,844)	(1,454)	4,381	1,504	3,003

7. Critical accounting estimates

In applying the Company's accounting policy, management is sometimes required to exercise accounting judgment with regard to estimates and assumptions which affect the amounts presented in the financial statements.

For information about critical accounting estimates, see Note 2 to the Company's interim financial statements as of September 30, 2008.

8. Linkage basis report

Below is the linkage basis report, on consolidated basis, as of September 30, 2008:

	In, or linked to the US dollar	In Israeli currency	In, or linked to the euro	In, or linked to the other currencies	Non-monetary items	Total
(in thousands US dollars)						
Assets						
Cash and cash equivalents	86,680	1,963	4,402	9,463	-	102,508
Short-term deposits	120,500	8,613	-	-	-	129,113
Trade receivables	120,570	439	14,316	16,456	-	151,781
Other receivables	26,708	7,984	1,055	2,553	-	38,300
Current derivative financial instruments	25,558	4,381	-	-	-	29,939
Prepaid expenses	-	-	-	-	25,958	25,958
Inventories	-	-	-	-	17,446	17,446
Long-term bank deposits	-	2,444	-	-	-	2,444
Investees	1,229	-	-	-	1,618	2,847
Investments in another company	1,581	-	-	-	-	1,581
Long-term derivative financial instruments	11	-	-	-	-	11
Fixed assets	-	-	-	-	1,282,454	1,282,454
Intangible assets	-	-	-	-	7,111	7,111
	382,837	25,824	19,773	28,472	1,334,587	1,791,493
Liabilities & Equity						
Short-term bank borrowings	(72,193)	(128)	(174)	(5)	-	(72,500)
Trade payables	(105,086)	(29,506)	(30,952)	(13,752)	-	(179,296)
Other payables	(34,822)	(6,049)	(3,342)	(2,249)	-	(46,462)
Provisions	(49,086)	(51,179)	-	-	-	(100,265)
Current derivative financial instruments	(21,239)	-	-	-	-	(21,239)
Current employee benefit obligations	(2,467)	(83,591)	(563)	(391)	-	(87,012)
Deferred income	-	-	-	-	(221,888)	(221,888)
Long-term loans from financial institutions	(668,339)	-	-	-	-	(668,339)
Long-term employee benefit obligations	(7,127)	(22,401)	(891)	(6,654)	-	(37,073)
Long-term loans from others	(188)	-	-	-	-	(188)
Long-term derivative financial instruments	(19,987)	-	-	-	-	(19,987)
Long-term provisions	(16,684)	-	-	-	-	(16,684)
Deferred tax	-	-	-	-	(53,967)	(53,967)
Shareholders' equity	-	-	-	-	(266,593)	(266,593)
	(997,218)	(192,854)	(35,922)	(23,051)	(542,448)	(1,791,493)
Monetary assets, net of monetary liabilities (monetary liabilities, net of monetary assets)	(614,381)	(167,030)	(16,149)	5,421	792,139	-

Free Translation of the Hebrew Language Financial Report - **Hebrew Wording Binding**

Below is the linkage basis report, on consolidated basis, as of September 30, 2007:

	In, or linked to the US dollar	In Israeli currency	In, or linked to the euro	In, or linked to the other currencies	Non-monetary items	Total
(in thousands US dollars)						
Assets						
Cash and cash equivalents	82,904	880	623	4,736	-	89,143
Short-term deposits	175,000	7,543	1,022	-	-	183,565
Trade receivables	136,544	61	15,316	19,488	-	171,409
Other receivables	20,956	5,820	-	1,599	-	28,375
Current derivative financial instruments	8,922	1,256	-	-	-	10,178
Prepaid expenses	-	-	-	-	26,845	26,845
Inventories	-	-	-	-	15,095	15,095
Long-term bank deposits	-	2,076	-	-	-	2,076
Investees	1,229	-	-	-	1,111	2,340
Investments in another company	1,865	-	-	-	-	1,865
Long-term derivative financial instruments	7,336	-	-	-	-	7,336
Fixed assets	-	-	-	-	1,293,511	1,293,511
Intangible assets	-	-	-	-	3,933	3,933
	434,756	17,636	16,961	25,823	1,340,495	1,835,671
Liabilities & Equity						
Short-term bank borrowings	(63,762)	(106)	(1,492)	(91)	-	(65,451)
Trade payables	(115,638)	(28,472)	(25,362)	(13,181)	-	(182,653)
Other payables	(38,255)	(4,567)	(3,142)	(1,930)	-	(47,894)
Provisions	(47,880)	(39,668)	-	-	-	(87,548)
Current employee benefit obligations	(2,442)	(71,771)	(551)	(367)	-	(75,131)
Deferred income	-	-	-	-	(197,266)	(197,266)
Long-term loans from financial institutions	(736,191)	-	-	-	-	(736,191)
Long-term employee benefit obligations	(24,063)	(16,916)	(6,465)	(4,030)	-	(51,474)
Long-term loans from others	(473)	-	-	-	-	(473)
Long-term derivative financial instruments	(225)	-	-	-	-	(225)
Long-term provisions	-	-	-	-	(61,982)	(61,982)
Deferred tax	-	-	-	-	(329,383)	(329,383)
Shareholders' equity	(1,028,929)	(161,500)	(37,012)	(19,599)	(588,631)	(1,835,671)
liabilities (monetary liabilities, net of monetary assets)	(594,173)	(143,864)	(20,051)	6,224	751,864	-

Free Translation of the Hebrew Language Financial Report - **Hebrew Wording Binding**

Below is the linkage basis report, on consolidated basis, as of December 31, 2007:

	In, or linked to the US dollar	In Israeli currency	In, or linked to the euro	In, or linked to the other currencies	Non-monetary items	Total
(in thousands US dollars)						
Assets						
Cash and cash equivalents	63,447	18,020	842	4,361	-	86,670
Short-term deposits	172,000	8,633	-	-	-	180,633
Trade receivables	99,917	422	20,653	22,625	-	143,617
Other receivables	12,263	3,912	4,235	1,844	-	22,254
Current derivative financial instruments	21,881	3,649	-	-	-	25,530
Prepaid expenses	-	-	-	-	25,096	25,096
Inventories	-	-	-	-	15,981	15,981
Long-term bank deposits	-	2,207	-	-	-	2,207
Investees	1,228	-	-	-	1,040	2,268
Investments in another company	1,715	-	-	-	-	1,715
Long-term derivative financial instruments	7,570	-	-	-	-	7,570
Fixed assets	-	-	-	-	1,285,752	1,285,752
Intangible assets	-	-	-	-	4,388	4,388
	380,021	36,843	25,730	28,830	1,332,257	1,803,681
Liabilities & Equity						
Short-term bank borrowings	(65,017)	(292)	(1,007)	-	-	(66,316)
Trade payables	(98,059)	(26,902)	(27,645)	(14,814)	-	(167,420)
Other payables	(37,492)	(3,783)	(3,492)	(2,418)	-	(47,185)
Provisions	(47,666)	(41,955)	-	-	-	(89,621)
Proposed Dividend payable	-	(3,008)	-	-	-	(3,008)
Current liability for employee benefits	(10,361)	(75,439)	(1,067)	(711)	-	(87,578)
Deferred income	-	-	-	-	(188,751)	(188,751)
Long-term loans from financial institutions	(713,793)	-	-	-	-	(713,793)
Long-term employee benefit obligations	(6,489)	(37,985)	(6,536)	(3,741)	-	(54,751)
Long-term loans from others	(423)	-	-	-	-	(423)
Long-term derivative financial instruments	(1,415)	-	-	-	-	(1,415)
Deferred tax	-	-	-	-	(64,576)	(64,576)
Shareholders' equity	-	-	-	-	(318,844)	(318,844)
	(980,715)	(189,364)	(39,747)	(21,684)	(572,171)	(1,803,681)
Monetary assets, net of monetary liabilities (monetary liabilities, net of monetary assets)						
	(600,694)	(152,521)	(14,017)	7,146	760,086	-

9. Disclosure in the Board of Directors' Report on the Matter of the Approval of the Financial Statements

The Company's controlling body is its Board of Directors.

Several committees operate in the framework of the Board of Directors, among them the Audit Committee, the Market Risk Management Committee, the Human Resources and Appointments Committee as well as the Finance, Budget and Balance Committee which numbers three members, among them a director from the public. The three committee members have accounting and financial capabilities as defined in the Companies Law of 1999 and the resulting regulations.

A draft of the Financial Statements is sent to the Board members for advance study.

The Finance, Budget and Balance Committee convenes for an extensive and in-depth discussion on the Financial Statement draft with the Company Auditor present. The CEO and CFO present the Financial Statements to the Committee members in great detail, including detailed financial analyses of the Company's performance in the reported period.

The Committee studies the material issues in the financial reporting, including material transactions not part of the regular course of business – in the event that such exist, the critical estimates and assessments implemented in the Financial Statements, the likelihood of the data, accounting policy implemented and changes thereof, if any, implementation of the full disclosure principle in the Financial Statements as well as various aspects of supervision and risk management.

When complex or essential issues are at stake, special Finance, Budget and Balance Committee meetings are held on the subject at hand, with the Auditor's participation.

The Committee holds discussions on the Financial Statements placed before it, which include questions addressed to the Company executives present and the Auditor. In addition, the Auditor is asked to present the Committee members with his remarks – if such exist, on subjects including the accounting policy implemented and special issues that arose throughout the audit. The committee reaches a decision to recommend that the Company's Board of Directors approve the Financial Statements, subject to modifications, changes and additions – if such are required by the Committee members.

The Financial Statements are presented to the Board members in a separate meeting, with the participation of the CEO, CFO and other senior Company executives as well as the Auditor.

In this forum as well, a discussion is held on the Statements, including questions addressed to the Auditor and to the Company's management, and the issues particular to the reported period are presented. The Board of Directors' decision whether to approve the Financial Statements is reached at the conclusion of discussions.

10. Explanation of the issue to which the Company's independent auditors draw attention in their review letter of the interim financial statements

The Company's independent auditors draw attention, in their review letter of the interim financial statements, to Note 5 of the interim financial statements with regard to legal proceedings against the Company.

Although the aforementioned issue does not cause any change to the standard independent auditors wording, attention must be drawn to it due to its potential material impact on the Company.

11. Disclosure regarding changes in the economic environment, impact of the capital market crisis and market risks.

- a. Towards the end of the third quarter and in the period since jet fuel prices and USD interest rates have continued to decrease and the NIS has devaluated vs. the USD. The impact these changes have had on the Company is detailed below.
- b. As of the balance sheet date (September 30 2008), the jet fuel price in the Mediterranean Basin Market was 284.0 cents per gallon. Following the balance sheet date, jet fuel prices dropped significantly and immediately prior to the approval of the quarter 3 2008 report (November 16 2008), the price was 184.4 cents per gallon.

The effective price the Company is expected to pay for fuel consumption (after hedging) in October is 12% lower than the effective price it paid in September 2008. An additional decrease of 10% is expected for November. Concurrently, the fair value of hedging devices and jet fuel is expected to drop as a result.

The Company is continuing to implement its hedging policy.

Following the drop in jet fuel prices the Company, as required by agreements with hedging institutions, provided interest-bearing guarantees to the amount of \$8 million for jet fuel hedging agreements open as of the financial statement date to the hedging institutions. This trend continued after the balance sheet date, and the Company provided additional guarantees as required. Note that the scopes of the guarantees change from day to day in accordance with jet fuel market prices and the Company makes daily calculations regarding changes needed to guarantees and their scope. The Company is negotiating with several banks for their provision of lines of credit for the issue of letters of credit for the Company for the aforementioned hedging agreements in return for liens on assets, this in lieu of deposits. The assets on which the Company intends to place liens in return for these credit lines are aircraft owned by the Company that are free of liens. As of these financial statements, the negotiations have yet to develop into an agreement with the banks. The Company estimates that appropriate solutions will be found for the release of deposits provided as guarantees for hedging institutions.

- c. Between the balance sheet date (September 30 2008) and a date immediately prior to the confirmation of the quarter 3 2008 report (November 16 2008), three-month LIBOR interest rates decreased by a rate of 45%.

The impact of the drop in LIBOR interest rates has on loan interest payments shall be expressed in the each loans next repayment date, meaning 2009 and onward. Interest repayments for Company loans for the fourth quarter of 2008 shall be made according to interest rates existing in previous quarters. The Company has hedging agreements for LIBOR rates (see Item 6.3 of the Board of Director Report above), the fair value of which is expected to drop following the drop in LIBOR interest rates.

- d. Between the balance sheet date (September 30 2008) and a date immediately prior to the confirmation of the quarter 3 2008 report (November 16 2008), the NIS was devaluated by 0.46 NIS relative to the USD.

The projected impact this devaluation will have as regards October 2008 is a \$2 million reduction of cash flow expenses compared to September 2008. Nevertheless, the Company has USD rate hedging agreements (see Item 6.4 of the Board of Directors' Report above), the fair value of which is expected to drop as a result of the NIS's devaluation relative to the USD.

In addition to the above, the NIS's devaluation in relation to the USD reduces the Company's NIS liabilities in USD terms (see Item 3.4 of the Board of Directors' Report above), thus reducing the Company's salary and financing expenses.

Note that the impact exchange rates will have on next quarter's business results shall be determined

based on exchange rates in effect throughout the quarter in its entirety and at its end (December 31, 2008).

12. Events occurring subsequent to the balance sheet date

As regards events occurring after the balance sheet date, see Note 10 of the September 30 Interim Financial Statements.

Prof. Israel (Izzy) Borovich
Chairman of the Board of Directors

Haim Romano
Chief Executive Officer

November 25, 2008

EL AL Israel Airlines Ltd.

Condensed Interim Consolidated Financial Statements
As of September 30, 2008

(Unaudited)

EL AL Israel Airlines Ltd.

Table of Contents

Page

CPA's Review Report

**Condensed interim consolidated financial statements
(unaudited) in USD:**

Consolidated Balance Sheets

Consolidated income statements

Statement of changes to shareholders' equity

Consolidated cash flow statements

Notes to condensed interim consolidated financial statements

To:
The Board of Directors,
EL AL Israel Airlines Ltd.
Ben-Gurion Airport

Dear Sir/Madam,

Re: Review of condensed interim consolidated financial statements (unaudited) as of September 30, 2008 and for the 9-month and 3-month periods then ended

At your request, we have reviewed the condensed interim consolidated financial statements of EL AL Israel Airlines Ltd. (hereinafter: "the Company") as of September 30, 2008, as well as the condensed interim consolidated income statements, statements of changes to shareholders' equity and consolidated cash flow statements for the 9-month and 3-month periods then ended.

Our review was conducted as per the procedures established by the Israeli CPA Association. These procedures included, inter alia: Reading the aforementioned financial statements; reading minutes of shareholder meetings and of meetings of the board of directors and its committees; and clarification sessions with people in charge of financial and accounting issues.

We have been provided with reports of other CPAs reviewing the condensed interim financial statements of consolidated companies whose assets constitute 0.9% of total assets included in the condensed interim consolidated balance sheet as of September 30, 2008, and whose revenues constitute 0.9% of total revenues included in the condensed interim consolidated income statements for the 9-month and 3-month periods ended September 30, 2008.

Since the review performed is of limited scope, and does not constitute a check under commonly accepted audit standards, we do not express our opinion of the summary interim financial statements.

Over the course of our review, including review of other CPA's reports, we have not become aware of any issue indicating that material changes would be required to the aforementioned financial statements in order for them to be deemed as proper interim financial statements in accordance with International Accounting Standard IAS 34 "Interim Financial Reporting" and in accordance with provisions of Chapter 4 of the Securities Regulations (Periodic and Immediate Statements), 1970.

We wish to draw your attention to Note 5 with regard to legal proceedings against the Company.

Sincerely yours,

Brightman Almagor & Co. CPAs

Tel Aviv, November 25, 2008

EL AL Israel Airlines Ltd.**Condensed consolidated balance sheet**

	<u>As of September 30</u>		<u>As of December 31</u>
	<u>2008</u>	<u>2007</u>	<u>2007</u>
	<u>Unaudited</u>		<u>Audited</u>
	<u>USD in thousands</u>		
<u>Assets</u>			
<u>Current assets</u>			
Cash and cash equivalents	102,508	89,143	86,670
Short-term deposits	129,113	183,565	180,633
Trade receivables	151,781	171,409	143,617
Other receivables	38,300	28,375	22,254
Derivative financial instruments	29,939	10,178	25,530
Prepaid expenses	25,958	26,845	25,096
Inventories	17,446	15,095	15,981
	<u>495,045</u>	<u>524,610</u>	<u>499,781</u>
<u>Non-current assets</u>			
Long-term bank deposits	2,444	2,076	2,207
Investment in affiliated companies	2,847	2,340	2,268
Investment in another company	1,581	1,865	1,715
Derivative financial instruments	11	7,336	7,570
Fixed assets	1,282,454	1,293,511	1,285,752
Intangible assets	7,111	3,933	4,388
	<u>1,296,448</u>	<u>1,311,061</u>	<u>1,303,900</u>
	<u>1,791,493</u>	<u>1,835,671</u>	<u>1,803,681</u>

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

EL AL Israel Airlines Ltd.**Condensed consolidated balance sheet**

	<u>As of September 30</u>		<u>As of December 31</u>
	<u>2008</u>	<u>2007</u>	<u>2007</u>
	<u>Unaudited</u>		<u>Audited</u>
	<u>USD in thousands</u>		
<u>Liabilities and shareholders' equity</u>			
<u>Current liabilities</u>			
Short-term borrowings and current maturities	72,500	65,451	66,316
Trade payables	179,296	182,653	167,420
Other payables	46,462	47,894	47,185
Provisions	100,265	87,548	89,621
Proposed dividend payable	-	-	3,008
Derivative financial instruments	21,239	-	-
Employee benefit obligations	87,012	75,131	87,578
Unearned revenues	221,888	197,266	188,751
	<u>728,662</u>	<u>655,943</u>	<u>649,879</u>
<u>Non-current liabilities</u>			
Long-term loans from financial institutions	668,339	736,191	713,793
Employee benefit obligations	37,073	51,474	54,751
Long-term loans from others	188	473	423
Derivative financial instruments	19,987	225	1,415
Long-term provisions	16,684	-	-
Deferred tax	53,967	61,982	64,576
	<u>796,238</u>	<u>850,345</u>	<u>834,958</u>
Total Liabilities	<u>1,524,900</u>	<u>1,506,288</u>	<u>1,484,837</u>
<u>Shareholders' equity</u>			
Share capital	155,012	155,012	155,012
Share premium	28,007	28,007	28,007
Capital reserve from transactions with a former controlling shareholder	237,122	236,351	237,122
Capital reserve in respect of share-based payment	5,472	3,940	4,464
Capital reserve in respect of cash flow hedging	(15,464)	2,556	8,341
Accumulated loss	(143,556)	(96,483)	(114,102)
	<u>266,593</u>	<u>329,383</u>	<u>318,844</u>
	<u>1,791,493</u>	<u>1,835,671</u>	<u>1,803,681</u>

Prof. Israel (Izzy) Borovich
Chairman of the Board of
Directors

Haim Romano
CEO

Nissim Malki
CFO

Ben-Gurion Airport, November 25, 2008
Certification date of interim financial statements

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

EL AL Israel Airlines Ltd.**Condensed interim consolidated income statement**

	For the 9-month period ended September 30		For the 3-month period ended September 30		For the year ended December 31
	2008	2007	2008	2007	2007
	Unaudited		Unaudited		Audited
	USD in thousands				
Operating revenues	1,635,761	1,408,156	607,273	566,715	1,932,450
Operating expenses	1,373,844	1,096,447	473,865	414,877	1,517,695
Gross profit	261,917	311,709	133,408	151,838	414,755
Selling expenses	180,434	159,552	63,865	65,967	230,886
General and administrative expenses	75,647	66,707	24,560	21,675	91,619
Other operating expenses (revenues), net	18,702	(4,174)	(5,412)	2,445	(2,423)
	274,783	222,085	83,013	90,087	320,082
Operating profit (loss) before finance cost/income	(12,866)	89,624	50,395	61,751	94,673
Finance cost	(37,964)	(37,578)	(12,029)	(15,842)	(56,062)
Finance income	18,313	11,068	1,986	4,504	19,469
Profit (loss) before tax	(32,517)	63,114	40,352	50,413	58,080
Income taxes	2,530	(13,135)	(10,402)	(9,720)	(13,586)
Profit (loss) after tax	(29,987)	49,979	29,950	40,693	44,494
Company's equity in earnings of affiliates, net	578	145	480	54	332
Profit (loss) for the period	(29,409)	50,124	30,430	40,747	44,826
Basic earnings (loss) per NIS 1 par value share, in USD	(0.06)	0.11	0.06	0.08	0.09
Number of shares used for calculation (in thousands) - basic	495,719	444,298	495,719	495,719	476,289
Diluted earnings (loss) per NIS 1 par value share, in USD	(0.06)	0.1	0.06	0.08	0.09
Number of shares used for calculation (in thousands) - diluted	495,719	495,721	495,719	495,719	495,934

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

EL AL Israel Airlines Ltd.**Condensed interim statement of changes to shareholders' equity**

	Share capital	Share premium	Capital reserve from transactions with former controlling shareholder	Capital reserve in respect of share-based payment	Capital reserve in respect of cash flow hedging	Accumulated deficit	Total
\$ in thousands							
The 9 months ended September 30, 2008 (unaudited):							
Balance as of January 1, 2008	155,012	28,007	237,122	4,464	8,341	(114,102)	318,844
Gain (loss) from cash flow hedges recognized directly in equity	-	-	-	-	⁽¹⁾ (23,805)	-	(23,805)
Loss for the period	-	-	-	-	-	(29,409)	(29,409)
Total recognized revenues and expenses	-	-	-	-	(23,805)	(29,409)	(53,214)
Benefit value of employee stock option program	-	-	-	1,008	-	-	1,008
Adjustments for dividends distributed	-	-	-	-	-	(45)	(45)
	-	-	-	1,008	-	(45)	963
Balance as of September 30, 2008	<u>155,012</u>	<u>28,007</u>	<u>237,122</u>	<u>5,472</u>	<u>(15,464)</u>	<u>(143,556)</u>	<u>266,593</u>
The 9 months ended September 30, 2007 (unaudited):							
Balance as of January 1, 2007	131,536	904	218,498	2,582	4,149	(146,607)	211,062
Gain from cash flow hedges recognized directly in equity	-	-	-	-	⁽²⁾ (1,593)	-	(1,593)
Net income for period	-	-	-	-	-	50,124	50,124
Total recognized revenues and expenses	-	-	-	-	(1,593)	50,124	48,531
Benefit value of employee stock option program	-	-	-	1,358	-	-	1,358
Receipts on account of Government of Israel debt	-	-	17,853	-	-	-	17,853
Exercise of option warrants into shares	23,476	27,103	-	-	-	-	50,579
	23,476	27,103	17,853	1,358	-	-	69,790
Balance as of September 30, 2007	<u>155,012</u>	<u>28,007</u>	<u>236,351</u>	<u>3,940</u>	<u>2,556</u>	<u>(96,483)</u>	<u>329,383</u>

(1) Net of tax impact amounting to \$8,148 thousand.

(2) Net of tax impact amounting to \$531 thousand.

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

EL AL Israel Airlines Ltd.**Condensed interim statement of changes to shareholders' equity**

	Share capital	Share premium	Capital reserve from transactions with former controlling shareholder	Capital reserve in respect of share-based payment	Capital reserve in respect of cash flow hedging	Accumulated deficit	Total
	\$ in thousands						
The 3 months ended September 30, 2008 (unaudited):							
Balance as of July 1, 2008	155,012	28,007	237,122	5,060	82,701	(173,986)	333,916
Gain from cash flow hedges recognized directly in equity	-	-	-	-	⁽¹⁾ (98,165)	-	(98,165)
Loss for the period	-	-	-	-	-	30,430	30,430
Total recognized revenues and expenses	-	-	-	-	(98,165)	30,430	(67,735)
Benefit value of employee stock option program	-	-	-	412	-	-	412
	-	-	-	412	-	-	412
Balance as of September 30, 2008	<u>155,012</u>	<u>28,007</u>	<u>237,122</u>	<u>5,472</u>	<u>(15,464)</u>	<u>(143,556)</u>	<u>266,593</u>
The 3 months ended September 30, 2007 (unaudited):							
Balance as of July 1, 2007	155,012	28,007	229,560	3,513	5,376	(137,230)	284,238
Gain from cash flow hedges recognized directly in equity	-	-	-	-	⁽²⁾ (2,820)	-	(2,820)
Net income for period	-	-	-	-	-	40,747	40,747
Total recognized revenues and expenses	-	-	-	-	(2,820)	40,747	37,927
Benefit value of employee stock option program	-	-	-	427	-	-	427
Receipts on account of Government of Israel debt	-	-	6,791	-	-	-	6,791
	-	-	6,791	427	-	-	7,218
Balance as of September 30, 2007	<u>155,012</u>	<u>28,007</u>	<u>236,351</u>	<u>3,940</u>	<u>2,556</u>	<u>(96,483)</u>	<u>329,383</u>

(1) Net of tax impact amounting to \$33,600 thousand.

(2) Net of tax impact amounting to \$940 thousand.

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

EL AL Israel Airlines Ltd.**Condensed interim statement of changes to shareholders' equity**

	Share capital	Share premium	Capital reserve from transactions with former controlling shareholder	Capital reserve in respect of share-based payment	Capital reserve in respect of cash flow hedging	Accumulated deficit	Total
	\$ in thousands						
For the year ended December 31, 2007 (audited)							
Balance as of January 1, 2007	131,536	904	218,498	2,582	4,149	(146,607)	211,062
Gain from cash flow hedges recognized directly in equity	-	-	-	-	⁽¹⁾ 4,192	-	4,192
Net income for the year	-	-	-	-	-	44,826	44,826
Total recognized revenues and expenses	-	-	-	-	4,192	44,826	49,018
Receipts on account of Government of Israel debt	-	-	18,624	-	-	-	18,624
Exercise of option warrants into shares	23,476	27,103	-	-	-	-	50,579
Benefit value of employee stock option program	-	-	-	1,882	-	-	1,882
Dividends distributed	-	-	-	-	-	(9,313)	(9,313)
Dividends declared	-	-	-	-	-	(3,008)	(3,008)
	23,476	27,103	18,624	1,882	-	(12,321)	58,764
Balance as of December 31, 2007	<u>155,012</u>	<u>28,007</u>	<u>237,122</u>	<u>4,464</u>	<u>8,341</u>	<u>(114,102)</u>	<u>318,844</u>

(1) Net of tax impact amounting to \$1,434 thousand.

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

EL AL Israel Airlines Ltd.**Summary interim consolidated cash flow statement**

	For the 9-month period ended September 30		For the 3-month period ended September 30		For the year ended December 31
	2008	2007	2008	2007	
	Unaudited		Unaudited		
	USD in thousands				
Cash flows from continuing operations					
Income (loss) for the period	(29,409)	50,124	30,430	40,747	44,826
Appendix A - Adjustments required for presentation of cash flow from current operations	127,258	152,333	(41,778)	35,200	210,704
	97,849	202,457	(11,348)	75,947	255,530
Deposit of proceeds from option warrant exercise in reserve for severance pay, for coverage of past liabilities	-	(24,376)	-	(1,864)	(24,376)
Net cash from current operations	<u>97,849</u>	<u>178,081</u>	<u>(11,348)</u>	<u>74,083</u>	<u>231,154</u>
Cash flow used for investment operations					
Acquisition of fixed assets (including general engine overhauls and payment on account of aircraft)	(93,764)	(221,245)	(30,025)	(183,761)	(248,558)
Proceeds from realized fixed assets	6,960	360	6,537	163	504
Investment in intangible assets	(3,267)	(446)	(523)	(358)	(644)
Increase in short-term deposits, net	51,520	(178,883)	66,582	(110,437)	(175,951)
Investment in deposits – service providers	(205)	(70)	(70)	(12)	(131)
Repayment of deposits – service providers	236	34	102	34	245
Investment in long-term deposits	-	(285)	-	(79)	(398)
Realized long-term deposits	82	157	82	28	225
Dividends received, net of share of affiliates' income	-	-	-	-	12
Repayment of investment in fixed assets	-	3,843	-	-	3,843
Net cash used in investment operations	<u>(38,438)</u>	<u>(396,535)</u>	<u>42,685</u>	<u>(294,422)</u>	<u>(420,853)</u>
Cash flow used in investment operations					
Proceeds from exercise of option warrants into shares	-	31,820	-	-	31,820
Long-term loans received from financial institutions	-	219,420	-	219,420	219,420
Long-term loans repaid to financial institutions	(39,575)	(79,540)	(17,228)	(60,694)	(101,267)
Other long-term loans received	-	-	-	-	98
Other long-term loans repaid	(292)	(1,861)	(92)	(627)	(2,309)
Payment in respect of loan-related expenses	-	(7,570)	-	(7,570)	(7,570)
Increase (decrease) in short-term credit, net	(653)	(830)	(1,058)	6	(668)
Dividends paid	(3,053)	-	-	-	(9,313)
Net cash from (used in) financing	<u>(43,573)</u>	<u>161,439</u>	<u>(18,378)</u>	<u>150,535</u>	<u>130,211</u>

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

operations

	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Increase (decrease) in cash and cash equivalents, net	15,838	(57,015)	12,959	(69,804)	(59,488)
Cash and cash equivalents balance at start of period	<u>86,670</u>	<u>146,158</u>	<u>89,549</u>	<u>158,947</u>	<u>146,158</u>
Cash and cash equivalents balance at end of period	<u><u>102,508</u></u>	<u><u>89,143</u></u>	<u><u>102,508</u></u>	<u><u>89,143</u></u>	<u><u>86,670</u></u>

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

EL AL Israel Airlines Ltd.**Condensed interim consolidated cash flow statement**

	For the 9-month period ended September 30		For the 3-month period ended September 30		For the year ended December 31
	2008	2007	2008	2007	2007
	Unaudited		Unaudited		Audited
	USD in thousands				
<u>Appendix A - Adjustments required for presentation of cash flows from regular operations</u>					
<u>Revenues and expenses not involving cash flow:</u>					
Depreciation and amortization (including disposal of accessories, disused components and consumables used)	96,698	100,693	32,433	34,529	135,777
Adjustment of value of long-term deposits	(268)	(112)	55	(130)	(198)
Share of income of affiliated companies	(579)	(60)	(481)	31	-
Deferred taxes, net	(2,274)	13,133	11,109	9,752	13,877
Increase (decrease) in liabilities in respect of employee benefits and in provisions	11,169	3,077	(8,439)	7,716	22,347
Net capital loss (gain) from realized fixed assets	(5,023)	1,514	(4,696)	(49)	1,440
Adjustment of value of other long-term loans	(14)	(13)	(6)	(9)	(20)
Adjustment of value of deposits for service providers	52	-	97	-	-
Benefit value of employee stock option program	1,008	1,358	412	427	1,882
Loss (gain) from adjustment of fair value of derivatives recognized in income statement	10,821	(15,113)	11,081	(624)	(19,867)
<u>Changes in asset and liability items:</u>					
(Increase) decrease in trade receivables	(8,164)	(38,865)	22,395	18,138	(11,073)
Decrease increase in other accounts receivable	(16,046)	(4,020)	(12,512)	(622)	2,100
Increase in prepaid expenses	(862)	(8,366)	7,961	4,208	(6,617)
(Increase) decrease in inventory	(1,465)	2,095	(671)	4,236	1,209
Increase in trade payables	11,876	37,663	(14,387)	21,405	22,430
Increase in other accounts payable	(2,808)	4,428	(20,380)	(10,355)	1,011
Increase in unearned revenues	33,137	54,921	(65,749)	(53,453)	46,406
	<u>127,258</u>	<u>152,333</u>	<u>(41,778)</u>	<u>35,200</u>	<u>210,704</u>
<u>Appendix B – Non-cash transactions</u>					
Government of Israel deposit to reserve for employee severance pay	-	17,853	-	6,791	18,624
Dividends declared and paid subsequent to the balance sheet date	-	-	-	-	(3,008)

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

Free Translation of the Hebrew Language Financial Report - **Hebrew Wording Binding**

Exercise of option warrants presented as liability	-	18,759	-	-	18,759
----------------------------------------------------	---	--------	---	---	--------

Appendix C – Cash payment of interest and taxes*

Interest payments	28,501	31,061	15,181	18,201	42,933
Interest receipts	(8,236)	(9,996)	(2,004)	(4,527)	(12,214)
Tax payments – advances in respect of extraneous expenses	97	60	20	20	244
Dividend receipts	-	-	-	-	345

* Reclassified

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

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

Note 1 - Significant accounting policies

a. Definitions

- The Company** - EL AL Israel Airlines Ltd.
- The Group** - The Company and its investee companies.
- Related parties** - As defined in IAS 24.
- Interested parties** - As defined in Securities Regulations (Compilation of Annual Financial Statements), 1993.
- Controlling shareholders** - As defined in the Securities Law, 1968 and regulations thereof.
- CPI** - The Consumer Price Index, as published by the Central Bureau of Statistics.
- USD** - US Dollar.
- Consolidated companies** - Companies in which the Company has control (as defined in IAS 27), directly or indirectly, whose financial statements are wholly consolidated with the Company's financial statements.
- Affiliated companies** - Companies in which the Company has material influence, and the Company's investment in which, directly or indirectly, is included in the financial statements based on the equity method.
- Investee companies** - Consolidated and affiliated companies.
- Other company** - A company owned by the Company in which the latter has no control or material influence.

b. Implementation of International financial reporting standards (IFRS)

- (1) Statement regarding implementation of International financial reporting standards (IFRS)

The Group's condensed interim consolidated financial statements (hereinafter: "Interim Statements") have been compiled in accordance with International Financial Reporting Standards (IFRS) and clarifications there to issued by the International Accounting Standards Board (IASB), as required for compilation of interim financial statements in accordance with IAS 34 "Interim financial reporting" (hereinafter: "IAS 34"). The

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

significant accounting policies listed below have been consistently applied for all reported periods presented in these condensed interim consolidated financial statements, as well as for compiling the opening balance sheet in accordance with IFRS, as set forth in section 2 below.

(2) Initial adoption of IFRS

In accordance with provisions of Accounting Standard no. 29 "Adoption of IFRS" by the Israeli Accounting Standards Board (hereinafter: "Standard 29"), starting on January 1, 2008, the Group applied IFRS and clarifications there to issued by the International Accounting Standards Board (IASB).

Therefore, these interim financial statements as of September 30, 2008 and for the 9-month and 3-month periods then ended, are compiled in accordance with IFRS and clarifications there to issued by the International Accounting Standards Board (IASB), as required for compiling condensed interim financial statements in accordance with IAS 34.

In these financial statements, the Company has applied provisions of IFRS 1 "Initial adoption of IFRS" (hereinafter: "IFRS 1"), which stipulate transition provisions for initial reporting in accordance with IFRS. In accordance with provisions of IFRS 1, the Group's transition date to IFRS-based reporting, as defined in IFRS 1, is January 1, 2007 (hereinafter: "the Transition Date"), and the balance sheet as of said date is the opening balance sheet in accordance with IFRS (hereinafter: "the Opening Balance Sheet").

In these interim financial statements, the Company has applied retroactively to all reported periods presented those IFRS standards issued by the compilation date of the interim consolidated financial statements, or which are expected to become effective y December 31, 2008. For easements elected by the Group in applying the transition provisions in accordance with IFRS 1 – see Note 9g below.

Prior to adopting IFRS, the Group compiled its financial statements in accordance with generally accepted accounting principles (GAAP) in Israel. The Company's latest annual financial statements in accordance with generally accepted accounting practices in Israel have been compiled as of December 31, 2007 and for the year then ended. The comparison figures for this period were re-stated in these financial statements in accordance with IFRS.

See Note 9 for material differences between IFRS-based reporting and Israeli GAAP-based reporting, inasmuch as these apply to the Group.

- (3) These interim financial statements are compiled in accordance with provisions of Chapter 4 of the Securities Regulations (Periodic and immediate reports), 1970 – with the exception of regulations which prohibit application of IFRS or of provisions allowed in accordance there with.
- (4) These condensed interim financial statements should be perused in conjunction with the Company's annual financial statements as of December 31, 2007 and for the year then ended, including their accompanying Notes, in as much as data included therein is not in contrast to financial statements which would have been included in accordance with IFRS.

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

c. Basis of preparation

These financial statements have been prepared on the historical cost basis except for the following:

- The following assets and liabilities, which are measured at fair value: financial instruments measured at fair value, derivative financial instruments.
- Non-current assets held for sale, presented at their carrying amount or at their fair value net of selling costs, whichever is lower.
- Inventory, presented at its cost or net realization value, whichever is lower.
- Fixed assets and intangible assets, presented at cost net of accumulated depreciation and amortization or at its recoverable amount, whichever is lower.
- Liabilities in respect of employee benefits, as set forth in Note 1v.

d. Foreign Currency

(1) Functional and presentation currency

The financial statements of each Group company are compiled in the currency of the major economic environment in which it operates (hereinafter: "the functional currency"). For the purpose of financial statement consolidation, the financial standing and results of each Group company are presented in USD, which is the Company's functional currency. The Company's consolidated financial statements are presented in USD. For exchange rates and changes thereto during the periods presented, see Note 1x.

An appendix to the financial statements provides a translation of the financial statements into NIS, as per provisions of IAS 21.

(2) Translation of transactions in currencies other than the functional currency

When compiling the financial statements of each Group company, transactions executed in currencies other than said company's functional currency (hereinafter: "Foreign Currency") are recorded at the exchange rates effective as of the transaction date. Upon each balance sheet date, monetary items denominated in foreign currency are translated using the exchange rate effective as of that date; non-monetary items measured at fair value and denominated in foreign currency are translated using the exchange rate effective as of the date on which fair value is determined; non-monetary items measured at historical cost are translated using the exchange rate effective as of the date of the transaction involving the non-monetary item.

(3) Recognition of exchange rate differentials

Exchange rate differentials are recognized in the income statement in the period in which they were generated.

e. Consolidated financial statements

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

The Group's consolidated financial statements include the financial statements of the Company and of entities directly or indirectly controlled by the Company. Control exists whenever the Company has the power to direct the financial and operational policies of an investee company in order to derive benefits from its operations.

For the sake of consolidation, all inter-company transactions, balances, revenues and expenses are fully eliminated.

f. Investments in affiliated companies

An affiliated company is an entity in which the Group has material influence and which is not a consolidated company. Material influence is the power to participate in decision making with regard to financial and operational policies of the affiliated company, which does not constitute control or joint-control of said policies.

Results, assets and liabilities of affiliated companies are included in the Company's consolidated financial statements based on the equity accounting method.

Gain or loss generated from transactions between the Company or a consolidated company and an affiliated company of the Group are eliminated based on the Group's share of rights in said affiliated company.

g. Cash and cash equivalents

Cash and cash equivalents include bank deposits available for immediate withdrawal as well as limited term deposits the use of which is unrestricted and whose term to maturity, at the time of investment, is up to three months.

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

h. Inventory

Inventory is presented at the lower of its cost and net realization value. The cost of inventory includes all purchasing cost and other cost incurred in getting the inventory to its current location and status.

Cost is determined using the weighted moving average method.

i. Fixed assets

Fixed assets are tangible items held for use in providing services or for leasing to others which are expected to be used for more than one period.

The Company presents its fixed asset items using the cost model as follows:

Fixed asset items are presented in the balance sheet at cost, net of accumulated amortization and net of accumulated impairment, if any. The cost included the acquisition cost of the asset, as well as cost which is directly attributable to getting the asset to the location and state required for its operation in the manner intended by management. The cost of qualifying assets also includes credit cost to be capitalized.

Fixed assets are amortized separately for each component of depreciable fixed asset item having a significant cost relative to the total item cost. Amortization is calculated systematically, using the straight line method over the expected useful life of the item components, starting on the date on which the asset is ready for its intended use, accounting for the expected residual value at the end of its useful life.

The following are depreciation rates for Company aircraft relative to cost (after deduction of residual value):

<u>Aircraft</u>	<u>Annual depreciation rate</u>
777	4.8%
747-400	5.7%
747-200	4.7%
767	8.0%
757	4.8%
737	4.2%

The cost of overhauling aircraft engines is recognized as an asset on the balance sheet, amortized over the period of economic benefit expected from said overhaul (based on estimated number of engine hours).

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

The residual value, amortization method and useful life of the asset are reviewed by Company management at the end of each fiscal year. Changes are treated as changes to estimates by means of "hence forward".

Assets under a financial lease are amortized over their expected useful life on equivalent basis of owned assets, or over the lease term if it is shorter.

For application of IAS 36 "Impairment of assets" – see Note 1k below.

Gain or loss generated from sale or obsolescence of an asset is determined by the difference between proceeds from its sale and its carrying amount, and is recognized in the income statement.

The cost of accessories and spare parts included with fixed assets is determined using the weighted moving average method.

Accessories and spare parts attributed to a specific fleet are amortized over the average remaining life time of said fleet. Accessories and spare parts not attributed to a specific fleet are amortized at a fixed annual rate.

Accessories and spare parts with no movement or slow movement are included at depreciated values according to management estimate.

j. Intangible assets

Rights for the use of security equipment are included at their cost to the Company, and are amortized using the straight line method based on the anticipated period of economic use, subject to impairment review. The lifetime estimate and amortization method are reviewed at the end of each reporting year, with the impact of changes to the estimate treated on hence-forward basis.

Software is included at its cost to the Company and is amortized using the straight line method based on its expected period of economic use.

k. Impairment of tangible and intangible assets

Upon each balance sheet date, the Group reviews the book value of its tangible and intangible assets in order to determine if there are any indications of impairment of said assets. If any such indications exist, the asset's recoverable amount is estimated in order to determine the impairment loss, if any. If the recoverable amount for a single asset cannot be estimated, the Group estimates the recoverable amount of the cash-producing unit to which the asset belongs.

The recoverable amount is the higher of the asset sale price less cost of sale and its use value. When estimating the use value, future cash flows are discounted to their present value using a pre-tax discount rate which reflects the current market estimates for time value of money and for asset-specific risks for which the future cash flow estimate has not been adjusted.

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

If the recoverable amount for an asset (or for a cash-generating unit) is estimated to be lower than its carrying amount, the carrying amount of the asset (or of the cash-generating unit) is depreciated down to its recoverable amount. Impairment loss is immediately recognized as an expense in the income statement.

Company management believes that recoverable amounts for aircraft should be reviewed relative to their amortized cost after grouping aircraft fleets, and that it is incorrect to review the recoverable amount of each aircraft individually relative to its amortized cost.

The Company, having grouped the aircraft fleets as set forth above, has determined that for each aircraft group, the recoverable amount exceeds the amortized cost of said aircraft group upon that date. Therefore, no provision for impairment of aircraft was made in these financial statements.

I. Financial assets

(1) General

Financial assets are recognized in the Group balance sheet when the Group becomes party to contractual terms of said instrument.

Investment in financial assets is initially recognized at cost, including transaction cost, except for financial assets recognized at fair value in the income statement, whose additional acquisition cost is recognized in the income statement.

The Group's financial assets are categorized as follows. This categorization depends on the nature and objective of the financial asset and is determined upon initial recognition of said financial assets:

- Financial assets measured at fair value in the income statement
- Loans and accounts receivable.

(2) Financial assets measured at fair value in the income statement

Financial assets are classified as "financial assets measured at fair value in the income statement" when such assets are held for trading or when they are designated as financial assets measured at fair value in the income statement.

A financial asset is classified as held for trading if it is a derivative neither designated nor effective as a hedging instrument.

The Group's financial assets under this category include derivative instruments not intended for use as hedging instruments, or which are not effective as such. These derivatives include certain derivatives based on the price of jet fuel, on interest rates and on exchange rates which are not designated as hedging instruments.

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

Financial assets measured at fair value in the income statement are presented at fair value. Any gain or loss due to change in fair value, including due to exchange rates, are recognized in the income statement in the period in which the change has occurred.

(3) Loans and accounts receivable

The Group's financial assets in this category include trade receivables, deposits and other accounts receivable at fixed or fixable installments which have no quote on an active market. Loans and accounts receivable are measured at amortized cost using the effective interest method, net of any impairment. Interest revenues are recognized using the effective interest method, except for short-term trade receivables and other accounts receivable – when interest amounts to be recognized in respect there of are not material.

(4) Impairment of financial assets

Financial assets, except for those classified as financial assets measured at fair value in the income statement, are reviewed for indications of impairment upon each balance sheet date. Such impairment occurs when there is objective evidence that expected future cash flow from investment in such asset has been negatively impacted due to one or more events which have occurred subsequent to initial recognition of the financial asset.

Indications of impairment may include:

- Significant financial challenges to debtor;
- Failure to make current principal or interest payments;
- Expectation that the debtor would become bankrupt or would re-structure their debt.

For financial assets presented at amortized cost, impairment is recognized as equal to the difference between the financial asset's carrying amount and the present value of future cash flow expected there from, discounted using its original effective interest rate.

If in a subsequent period, the loss due to impairment of a financial asset decreases, and said decrease is objectively related to an event occurring after recognition of impairment, then the impairment loss previously recognized is reversed, in whole or in part, in the income statement. Such reversal is limited in amount, so that the carrying amount of investment in the asset upon reversal of impairment loss would not exceed the amortized cost of the asset as of that date - had no impairment been previously recognized.

As for trade receivables, their carrying amount is decreased, if necessary, using a provision for doubtful debt. The provision is specifically calculated. When trade receivables are not collectable, they are written off against the provision account. Collection, in subsequent periods, of

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

amounts previously written off is credited against the provision account. Changes in carrying amount of the provision account are recognized in the income statement.

m. Financial liabilities and equity instruments issued by the Group

(1) Classification as financial liability or equity instrument

Non-derivative financial instruments are classified as a financial liability or as an equity instrument, based on the nature of their underlying contractual terms.

An equity instrument is any contract indicating a residual right to Group assets, after deduction of all Group liabilities. Equity instruments issued by the Company are stated at their issuance proceeds net of expenses directly related to issuance of said instruments.

Group financial liabilities are stated and measured based on the following classification:

- Financial liabilities measured at fair value in the income statement.
- Other financial liabilities.

(2) Option warrants for purchase of Company shares

Proceeds from issuance of option warrants for purchase of Company shares, which confer upon their owners the right to purchase a set number of ordinary shares in return for a variable cash amount, are stated under current liabilities and are classified as liabilities measured at fair value in the income statement. As the Company has issued option warrants whose exercise price is not denominated in its functional currency (the exercise price is NIS-denominated and linked to the Consumer Price Index), the exercise price is deemed to be a variable amount.

(3) Financial liabilities measured at fair value in the income statement

Group financial liabilities in this category include certain interest rate and exchange rate derivatives not designated as hedging instruments, as well as option warrants for purchase of Company shares, as set forth above.

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

Financial liabilities measured at fair value in the income statement are stated at fair value. Any gain or loss due to change in fair value is recognized in the income statement. Transaction costs are charged to the income statement upon initial recognition.

(4) Other financial liabilities

Other financial liabilities include credit and loans, trade receivables and other accounts receivable. Such liabilities are initially recognized at fair value, net of transaction costs. Subsequent to initial recognition, other financial liabilities are measured at amortized cost using the effective interest method.

n. Derivative financial instruments and hedging accounting

(1) General

The Company uses a range of derivative financial instruments to manage exposure to changes in price of jet fuel, interest rates and foreign currency exchange rates.

Derivative financial instruments are initially recognized at their fair value upon the contracting date and at each subsequent balance sheet date. Changes to the fair value of derivative financial instruments are generally recognized in the income statement. The timing of recognition in the income statement of changes in fair value of derivative financial instruments designated as hedging, when such hedging is effective and meets all conditions for qualification as a hedging relationship, depends on the nature and type of hedging, as set forth below.

The balance sheet classification of derivative financial instruments is determined based on the contractual term of the derivative financial instruments. If the remaining contractual term of the derivative is longer than 12 months, the derivative is stated as a non-current item on the balance sheet; if the remaining term is shorter than 12 months, the derivative is classified as a current item.

(2) Hedge accounting

The Company applies cash hedge accounting, and to this end it has designated certain derivative financial instruments in respect of exposure to jet fuel prices and to interest rate changes.

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

In order to hedge jet fuel prices, the Company has entered into multiple transactions in respect of expected fuel purchases for terms of up to 2 years from the balance sheet date.

In order to reduce exposure to adjustable interest rates applicable to Company loans, the Company has entered into multiple contracts designated to fix interest rates. Interest hedging instruments used by the Company are aligned with repayment schedules of the loans they are designated to hedge in the related periods.

The hedging relationships are documented by the Company upon contracting the hedging transaction. This documentation identifies the hedging instrument, hedged item, hedged risk, hedging strategy applied as well as a review of the fit of this strategy to overall Group policy for each hedge type. Furthermore, starting on the start date of hedge relationship and throughout its term, the Company documents the degree to which the hedging instrument is effective in offsetting exposure to changes in cash flow due to the hedged risk for the hedged item.

The effective portion of changes in value of financial instruments designated as cash flow hedges is immediately recognized in equity under "Capital reserve in respect of cash flow hedging", and the non-effective portion is immediately recognized in the income statement.

Cash flow hedge accounting is discontinued when the hedging instrument expires, is sold or realized or when the hedging relationship no longer meets the minimum hedging conditions. Subsequent to discontinuation of hedge accounting, the amounts recognized in shareholders' equity are recognized in the income statement when the hedged item or the hedged anticipated transactions are recognized in the income statement.

o. Revenue recognition base and commission attribution to agents

- (1) Revenues from sale of flight tickets are included as unearned revenues under current liabilities until the service is provided or up to 2 years from the sale date, whichever is earlier.

Air passenger revenues also include revenues where the service is provided by the Company, whereas flight tickets are sold by other airlines.

Furthermore, air passenger revenues also include revenues due to code share agreements with other airlines. In such cases, when the service is provided by the other airlines, whereas the sale is made by the Company - revenues are stated on net basis.

- (2) Air cargo revenues are recognized in the income statement when the service is provided.
- (3) Agent commissions referring to revenues not yet recognized are included in the financial statements under "pre-paid expenses", and will be recognized as selling expenses in the income statement concurrently with revenue recognition.
- (4) Interest revenues are accumulated periodically, accounting for the principal to be repaid and using the effective interest method.

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

p. Engine maintenance and refurbishment expenses

Maintenance and engine refurbishment expenses (not constituting an overhaul) as set forth above in Note 1i are recognized in the income statement upon actual execution of the engine maintenance or refurbishment work.

In cases where the Company has entered into agreements of an insurance nature, the Company records expenses as specified in the insurance agreements, and the cost of refurbishment is incurred by the insurer.

q. Expenses for securing Company services

Company contribution to government expenses for securing company services are recognized in the income statement when incurred, based on the Company's share of said expenses.

r. Leases

(1) General

Lease agreements are classified as financial leases when terms of the contract transfer all material risk and rewards arising from ownership to the lessee. Other leases are classified as operational leases.

(2) Rental fee expenses in respect of operational leases (primarily aircraft leases) are recognized based on the straight line method over the term of the lease. In lease agreements where no leasing fee, or a reduced leasing fee, is paid at the start of the leasing period and where other benefits are obtained from the lessor, the Company recognizes expenses based on the straight line method over the lease term.

s. Provisions

(1) General

Provisions are recognized when the Group has a legal or implied obligation due to a past event, where use of reliably measurable economic resources is expected to discharge the said obligation.

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

The amount recognized as provision reflects management's best estimate of the amount to be required for settling the current obligation upon the balance sheet date, accounting for risk and uncertainty associated with said obligation. When the provision is measured using expected cash flows for settlement of the obligation, the carrying amount of the provision is the present value of expected cash flows. The interest rate used by the Company to discount a provision in respect of an inquiry by the US Antitrust Division (as set forth in Note 5b1) is 3.7%.

When the amount required to settle the current obligation, in whole or in part, is expected to be reimbursed by a third party, the Group recognized an asset, in respect of said reimbursement, up to the amount of the provision recognized, only when it is virtually certain that such indemnification would be received and when it may be reliably measured.

(2) Liabilities in respect of frequent flyer programs

The provision is calculated using the estimated effective cost to the Company arising from usage of benefits conferred under these programs, using the estimated likelihood of benefit utilization. The effective cost is based on estimated relative weight, according to management, of marginal expenses which the Company may incur, and of loss of alternative revenues due to rejection of paying passengers upon realization of the aforementioned benefits.

For publication of IFRIC 13, see Note 1y1c.

(3) Lawsuits

These financial statements include appropriate provisions with regard to lawsuits filed against Group companies which Group management believes would not be rejected or eliminated, although Group companies contest these claims.

These lawsuits are treated in accordance with IAS 37. Pursuant to these provisions, provisions are included in respect of claims likely to materialize (probability higher than 50%), which Group management believes, based on advice of legal counsel, to be appropriate to the circumstances of each and every case.

t. Share-based payments

Share-based payments to employees, settled using Group equity instruments, are measured at fair value upon their grant date. The Company measures, upon the grant date, the fair value of equity instruments granted by using the Black & Scholes model. When the granted equity instruments do not vest until employees complete a specified period of service, the Company recognizes the share-based payment agreements in its financial statements over the vesting period against an increase in shareholders' equity, under "Capital reserve in respect of share-based payment". Upon each balance sheet date, the Company estimates the number of equity instruments expected to vest. Change in estimate relative to prior periods is recognized in the income statement over the remaining vesting period.

u. Taxes on revenue

(1) General

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

Expenses (revenues) in respect of taxes on revenue include all current taxes, as well as total change in deferred tax balances, except for deferred taxes arising from transactions recognized in equity.

(2) Current taxes

Current tax expenses are calculated based on taxable revenue of the Company and consolidated companies during the reported period. The taxable revenue differs from income before taxes on revenue, due to inclusion or exclusion of revenue and expense items which are taxable or deductible in different reporting periods, or which are not taxable or deductible. Assets and liabilities in respect of current taxes were calculated based on the tax rates and taxation legislation enacted, or effectively enacted, by the balance sheet date.

(3) Deferred taxes

Group companies generate deferred taxes in respect of temporary differences between the value of assets and liabilities for tax purposes and their carrying amount in the financial statements. The deferred tax balances (assets or liabilities) are calculated using the tax rates expected upon their realization, based on the tax rates and taxation legislation enacted, or effectively enacted, by the balance sheet date. Deferred tax liabilities are usually recognized in respect of all temporary differences between the value of assets and liabilities for tax purposes and their carrying amount in the financial statements. Deferred tax assets are recognized in respect of all deductible temporary differences up to the amount for which taxable revenue is expected to allow for utilization of the deductible temporary difference.

In calculating deferred taxes, taxes which would apply in case of realization of investments in investees are not accounted for, since the Group intends to hold and develop said investments. In addition, the Company did not account for deferred taxes for profit distribution in said companies, since dividends are tax exempt.

Deferred tax assets and liabilities are stated on offset basis, when an enforceable legal right exists to offset tax assets against tax liabilities, and when they refer to taxes on revenue imposed by the same tax authority, where the Group intends to settle the tax assets and liabilities on net basis. The Company and several consolidated companies are jointly assessed for taxes on revenue, therefore deferred tax assets and deferred tax liabilities of said companies are presented on offset basis.

v. Employee benefits

(1) Post-employment benefits

Post-employment benefits at the Group include: pensions, severance pay liability, adjustment pay to executives, redemption of sick pay and certain benefits to Company retirees. Some post-employment Company benefits are defined contribution plans and some – defined benefit plans.

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

Expenses in respect of Company liability to deposit funds to a defined contribution plan are recognized in the income statement upon provision of employment services for which the Company is liable to make said deposit.

Expenses in respect of defined benefit plans are recognized in the income statement based on the projected unit credit method, using an actuarial estimation prepared upon each balance sheet date. The present value of Company obligations in respect of defined benefit plans is determined by discounting expected future cash flows expected from the plan using market yield of government bonds denominated in the currency in which plan benefits are to be paid, and having a term to maturity approximately equal to the expected plan settlement date.

Actuarial gain or loss in excess of 10% over the present value of the obligation in respect of a defined benefit plan and the fair value of plan assets as of the start of the period, whichever is higher, are amortized over the remaining average service duration expected for employees who participate in the plan.

Company liability in respect of a defined benefit plan, presented on the Company balance sheet, includes the present value of the liability in respect of defined benefit, plus actuarial gain (less actuarial loss) yet to be realized, net of the fair value of plan assets.

(2) Other long-term employee benefits

Other long-term employee benefits are benefits expected to be utilized or payable in a period over 12 months from the end of the period in which the service qualifying for the benefit was rendered.

Other employee benefits at the Company include part of the liability in respect of paid leave and the anniversary bonus. These benefits are recognized in the income statement using the Projected Unit Credit Method, using actuarial estimates prepared upon each balance sheet date. The present value of Company obligations in respect of these investments is determined by discounting expected future cash flows expected from the plan using market yield of government bonds denominated in the currency in which benefits are to be paid, and having a term to maturity approximately equal to their expected settlement date.

Actuarial gain and loss in respect of other long-time employee benefits are recognized in the income statement when generated.

(3) Short-term employee benefits

Short-term employee benefits are benefits expected to be utilized or payable in a period within 12 months from the end of the period in which the service qualifying for the benefit was rendered.

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

Short-term employee benefits at the Company include Company liability in respect of wages, bonuses and part of the liability in respect of paid leave. These benefits are recognized in the income statement when generated. The benefits are measured on a non-capitalized basis. The difference between the short-term benefits to which an employee is eligible and the amount paid for them is recognized as a liability.

(4) Early retirement plans

Company liability in respect of early retirement plans are recognized in the income statement when the Company is committed to a formal employment termination plan, including, at least, the site, position and estimated number of employees to be terminated, the benefits to which terminated employees are eligible and the date on which the plan would be executed. Furthermore, the time until implementation is complete should be such that material changes to the plan are unlikely. The benefit amount is determined using the discount rate for government bonds.

w. Earnings per share

The Company calculates basic earnings per share, for income or loss attributed to holders of Company shares by dividing the income or loss attributed to holders of Company ordinary shares (the numerator) by the weighted average number of ordinary shares outstanding (the denominator) during the reported period. In order to calculate diluted earnings per share, the Company adjusts the earnings or loss attributed to holders of ordinary shares, and the weighted average number of shares outstanding, for impact of all potentially dilutive shares.

x. Exchange rates and linkage basis

(1) Balances in foreign currency, or linked to foreign currency, are included in financial statements according to official exchange rates published by the Bank of Israel as of the date of the balance sheet.

(2) Balances linked to the Consumer Price Index are presented using the most recent known CPI value upon the balance sheet date.

(3) Below are data for USD exchange rates and CPI in Israel:

	As of September 30		As of December 31
	2008	2007	2007
CPI (in points)	199.5	189.1	191.2
USD/NIS exchange rate	3.421	4.013	3.846
USD/EUR exchange rate	0.684	0.705	0.680

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

Change in %:

	For the 9-month period ended September 30		For the 3-month period ended September 30		For the year ended December 31
	2008	2007	2008	2007	2007
Consumer Price Index	4.3	2.3	1.9	1.3	3.4
USD/NIS exchange rate	(11.1)	(5.0)	2.1	(5.6)	(9.0)
USD/EUR exchange rate	0.6	(7.1)	7.9	(5.2)	(10.4)

y. New financial reporting standards and clarifications published

- (1) Information regarding standards, standard revisions and clarifications published and which are not yet effective, which the Company has not adopted by means of early adoption, which may be applicable to the Group -

(a) IAS 1 (Revised) – Presentation of Financial Statements

The standard sets forth the presentation required in financial statements, and provides details of a general framework for the outline of a financial statement as well as the minimum content to be included in such statement. In the revision of these standards, changes were made to the current presentation format of financial statements, and presentation and disclosure requirements with regard to financial statements have been expanded, including presentation of an additional statement included in the financial statements, named "statement of comprehensive income", as well as the addition of a balance sheet as of the start of the earliest period presented in the financial statements in case of change in accounting policy by means of retroactive application, in cases of re-statement and in cases of re-classification.

The standard will apply to reporting periods starting on January 01, 2009. The standard allows for early adoption.

At this time, Group management is unable to estimate the impact of application of this standard on its financial statements.

(b) IFRS 8 - Operating Segments

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

The standard, which supersedes IAS 14, sets forth how a corporation is to report information by segment in its annual financial statements. *Inter alia*, the standard stipulates that the company's segment reporting shall be based on information used by company management for evaluation of segment performance, and for making decisions with regard to resource allocation to the different operating segments. The standard would apply for annual reporting periods starting on January 01, 2009 with retroactive adjustment of comparison figures for prior reporting periods. The standard allows for early adoption.

(c) IFRIC 13 – Customer Loyalty Programs

This clarification stipulates that transaction for sale of flight tickets, wherein the company awards its customers with points in a frequent flyer club, which may be used in the future for flight tickets, shall be treated as multi-component transactions, and the payment received from the customer will be allocated to its different components based on the fair value of the credit award. The proceeds attributed to the award shall be recognized as revenue when the credit awards are cashed and the company is liable to provide the rewards.

Provisions of this clarification apply to annual reporting periods starting on January 01, 2009. Early adoption is possible.

At this Group management is unable to estimate the impact of implementation of this clarification on its financial standing and operating results.

(d) Improvements to International Financial Reporting Standards 2008

In May 2008, the IASB published a series of improvements to International Financial Reporting Standards.

These improvements include revisions to some of the standards, which modify the way different items are stated, recognized and measured in the financial statements.

Furthermore, some terminology corrections were made which have a negligible impact, if any, on the financial statements.

Most of the revisions will become effective starting on annual reporting periods starting on January 01, 2009 or later, with optional early adoption. Most of the revisions would be applied by way of retroactive adjustment of comparison figures.

These revisions include several revisions which, under applicable circumstances, may impact the financial statements. The main such revisions are new or revised requirements with regard to:

- Revision of IFRS 5 "Non-current assets held for sale and discontinued operations" which stipulates that company assets and liabilities will be classified as held for sale when the parent company is committed to execute a plan to sell controlling rights to the company, even when it intends to maintain rights which do not confer control.

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

Company management estimates that application of this revision would have no impact on Group financial statements.

- Revision to IAS 28 "Investments in Associates", which stipulates that impairment of an investment in an associate will be treated as impairment of a single asset, and that the impairment amount may be reversed in subsequent periods.

This revision will apply to annual reporting periods starting on January 01, 2009. The revision allows for early adoption, including application of revisions referring to section 4 of IAS 32 "Financial Instruments: Presentation", to section 1 of IAS 31 "Interests in Joint Ventures" and to section 3 of IFRS 7 "Financial Instruments: Disclosures". This revision may be applied by means of "hence forward".

Company management estimates that application of this revision would have no impact on Group financial statements.

- Revision of IAS 38 "Intangible Assets", which stipulates that payments for advertising and sales promotion activities shall be recognized as an asset until the date on which the entity has access to goods purchased, or in case of services – the date said services are rendered.

This revision will apply to annual reporting periods starting on January 01, 2009. This revision will be applied retroactively. This revision allows for early adoption.

At this time, Group management is unable to estimate the impact of application of this revision on its financial statements.

- (e) In May 2008, the IASB published revisions to IFRS 1 and to IAS 27 "Consolidated Financial Statements".

In these revisions, a company initially adopting IFRS may use "deemed cost" for stating investment in investees in the company's solo financial statements upon the transition date to international standards. Furthermore, the requirement with regard to dividends received in respect of investment stated at cost has been modified, such that said dividends would always be recognized in the income statement.

The aforementioned revisions will become effective with annual financial statements for periods starting on January 01, 2009. Early adoption is possible.

The Company is reviewing potential implications of the aforementioned revisions.

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

- (2) Below are details of standards, revisions and clarifications published and which are not yet in effect, which may apply to the Group:
- (a) Revision to IFRIC 2 "Share-based Payments – Vesting Conditions and Cancellations".
 - (b) IFRIC 15 "Agreements for Construction of Real Estate".
 - (c) IFRIC 16 "Hedges of a Net Investment in a Foreign Operation".
 - (d) IAS 23 (Revised) "Borrowing Costs".
 - (e) IFRS 3 (Revised) "Business Combinations".

Note 2 - Key sources for estimates of uncertainties

a. General

In applying Group accounting policy, as set forth in Note 1 above, company management is sometimes required to exercise considerable judgment with regard to estimates and assumptions about the carrying amount of assets and liabilities, which may not be available from other sources. These estimates and related assumptions are based on past experience and other factors deemed relevant. Actual results may differ from these estimates.

Estimates and underlying assumptions are regularly reviewed by management. Changes in accounting estimates are only recognized in the period in which a change was made to the estimate, if the change only affects that period, or are recognized in said period and in subsequent periods in cases where the change affects both the current period and the subsequent periods.

b. Key sources for estimates of uncertainties

(1) Provisions for legal proceedings

As of September 30, 2008, there are claims pending against the Company amounting to a total of \$370 million. In addition, there are claims not quantified in monetary terms. A provision was made in respect of some of these claims in the amount of \$24.8 million. (The aforementioned claim and provision amounts exclude tax assessments issued to the Company – see sub-section 3 below). In order to review of the legal validity of the aforementioned claims, as well as to determine the probability of their realization to the Company's detriment, Company management relies on the opinion of legal and professional counsel. After the Company's counsel have formed their legal opinion and the Company's probability with regard to the claim subject, whether the Company would have to bear its outcome or may postpone it, Company management

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

estimates the amount to be included in the financial statements, if any. Interpretation by the Company of the current legal position which differs from that of its legal counsel, different understanding by Company management of contracts as well as changes due to applicable legislation or addition of new facts – all may impact the value of the overall provision for legal proceedings pending against the Company, thereby materially impacting its financial standing and operating results.

(2) Taxes on income

The company has tax assessments for which the tax consequences are uncertain. The Company recognized liabilities in respect of tax consequences of these transactions, based on Management estimates, which rely on professional counsel with regard to timing and amount of the tax liability which may arise there from. When the tax consequence of such transactions differs from Management estimates, tax expenses would differ upon determination of the final assessment.

(3) Employee benefits

The present value of the Company's severance pay liability, as well as that of a pension plan and other employee benefits, is based on multiple data determined based on actuarial estimate, using multiple assumptions, including with regard to discount rate. Changes in actuarial assumptions may impact the carrying amount of the Company's severance pay and pension liabilities. The Company estimates the discount rate annually, based on the discount rate for government bonds. Other key assumptions are made based on prevailing market conditions, as well as on the Company's past experience. For further details of assumptions made by the Company, see Note 1v.

(4) Aircraft impairment

As set forth in Note 1k above, for any aircraft fleet where indications of impairment exist, the Company estimates the recoverable amount for said fleet. The recoverable amount is the higher of the aircraft sale price and its use value. In estimating the use value, the Company estimates the future cash flows, discounting them to their present value using a discount rate which reflects current market estimates. In so doing, the Company has relied on forecasts related, *inter alia*, to expected scope of operations, prices of flight tickets and of bills of lading, operating cost and future interest rates. Material changes to these estimates, or part thereof, may impact the recoverable amount of said aircraft.

(5) Liabilities in respect of frequent flyer clubs

The provision for frequent flyer clubs is calculated using the estimated effective cost to the Company arising from usage of benefits conferred under these programs, using the estimated likelihood of benefit utilization. The effective cost is based on estimated relative weight, according to

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

management, of marginal expenses which the Company may incur, and of loss of alternative revenues due to rejection of paying passengers upon realization of the aforementioned benefits.

Note 3 - **Seasonality**

Passenger traffic at Ben Gurion airport is highly seasonal. Most of the activity is in the summer months, with the peak being in July-September. Winter months (January-March) show reduced passenger traffic.

Note 4 - **Fixed assets**

- a. On March 16, 2008, the Company signed an agreement with Boeing Corp., whereby it would acquire from Boeing four new 777-200 ER aircraft.

These aircraft, to be equipped with Rolls Royce engines, are expected to join the Company's mid- and long-range passenger aircraft fleet, with a 279 seat configuration. These aircraft will be delivered to the Company in January 2012, April 2012, November 2012 and January 2013.

Total acquisition cost for the four aircraft, including spare parts and required installations to adapt them to Company needs, amounts to \$540 million.

According to the agreement with Boeing, payment for each aircraft will only start two years prior to its scheduled delivery date to the Company. Therefore, at this time the Company has yet to make a final decision with regard to financing of this transaction, and the Company is reviewing its options.

Pursuant to terms of this agreement, the Company was granted an option to convert the aforementioned acquisition into new 777-300 ER aircraft (to be equipped with General Electric engines), with a 348 seat configuration. The Company may exercise its option no later than December 31, 2008. Exercise of said option involves changes to terms of the agreement, but aircraft delivery dates would remain unchanged.

Furthermore, the agreement grants the Company another option to acquire two additional such aircraft, to be delivered to the Company in 2014 and 2015, in accordance with terms set forth in the agreement.

On April 30, 2008, the Company Board of Directors approved the aforementioned agreement. During the reported period, the Company made down payments for the aforementioned aircraft amounting to \$10.6 million (of which \$9.6 million in Q2 of 2008). Furthermore, for the option to acquire two additional aircraft, the Company paid a further \$2 million in Q2.

The Company is reviewing its current fleet and the required adjustments there to in view of the aforementioned agreement, other agreements to acquire aircraft (as reported by the Company) and its "EL AL 2010" business strategy.

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

- b. On April 10, 2008, the Company signed an agreement with a Spanish airline, whereby 3 new 737-800 aircraft would be acquired. The aircraft are expected to be delivered in 2009. Total investment for acquisition of these 3 aircraft, including expected cost for putting them into service for the Company, is estimated at \$145 million. Self-financing is expected to amount to 15% of aircraft cost, with the balance financed by loans.

The aforementioned acquisition is in line with the Company's business strategy to gradually renew its aircraft fleet, in accordance with principles of the "EL AL 2010" strategic plan.

In the reported period, the Company paid \$19 million on account of these three aircraft (of which \$4 million was paid in Q3 of 2008). Additionally, the Company paid a total of \$1.4 million to Boeing in the reported period for adaptation of the aircraft in question to the Company's needs.

In August 2008 a new 737-800 airplane was added to the Company's passenger fleet, the first of five aircraft of this model intended for the El Al fleet. The aircraft was leased for a nine-year period and contains 142 seats. An additional new plane of the same type was intended to be delivered in October 2008, but as a result of a strike at Boeing, the aircraft's manufacturer, its delivery to the Company has been postponed. Monthly leasing fees for the first plane mentioned above amount to \$376 thousand.

- c. On January 10, 2008, the Company signed an agreement to acquire a 747-400 passenger aircraft. The aircraft was manufactured in 1994, and was delivered to the Company in October 2008.

The Company paid the entire proceeds for the purchase of the aircraft, investments for its adoption at the Company and costs of additions and installations needed to be carried out on the plane so as to adapt it to the Company's needs, a total of some \$50 million, after the balance sheet date.

Self financing amounted to \$14 million, with the balance financed by loans, to the amount of \$36 million, in accordance with a long-term credit agreement with a foreign bank.

Acquisition of this aircraft is in line with the Company's "EL AL 2010" business strategy, whereby the Company continues to review its procurement needs.

- d. On July 17 2008 the Company signed an agreement for the sale of two Boeing 767-200 airplanes, manufactured in 1983, owned by the Company. The delivery of one 767-200 to a Philippine airline was completed on October 15 2008, this after the entire proceeds for this aircraft, a total of \$6.5 million U.S., had been paid to the Company prior to the signing of the agreement. As regards the sale of the second 767-200, the intended purchaser, a Singapore investment company, informed the Company that it would be unable to meet payments for the aircraft due to difficulties in securing bank financing and therefore would be unable to purchase it, leaving the \$325 thousand advance payment in the Company's possession.

The Company listed a pre-tax revenue of \$4.7 million U.S. for the sale of the plane in its third quarter financial statements.

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

These transactions have been conducted pursuant to the examination of the Company's existing fleet and business strategy, "El Al 2010", which deals with, among other things, the replacement and refreshing of the fleet.

Note 5 - **Legal Proceedings**

a. Class action suits

In previous years, two claims were filed against the Company and awarded class action status by Courts of Law:

- (1) In October 1998, a claim against the Company was filed with the Nazareth District Court, along with a motion for class action status, amounting to NIS 230.4 million (\$67 million as of the balance sheet date). The claim makes reference to allegations of over-charging for flight tickets by travel agents due, according to the plaintiff, to use of inappropriate exchange rates. In 2002, the Court granted class action status to this lawsuit, for causes arising from the Consumer Protection Act. The Company filed a motion to appeal to the Supreme Court. Company management believes, based on opinion of its legal counsel, that the Company is not expected to be liable for this lawsuit. No provision was made in these financial statements in respect of this claim.
- (2) In September 1999, a claim was filed with the Tel Aviv District Court against the Company, against the Airport Authority and against Ophir Tours (a travel agency), along with a motion for class action status, amounting to NIS 21.7 million (\$6 million as of the balance sheet date). The plaintiff claims that the travel agent charged it with a passenger fee using an exchange rate higher than legally allowed for this purpose, which is the representative exchange rate, and that the Company is also liable for deeds of travel agents on this matter. In 2002, the Court granted class action status to this claim with regard to violation of a statutory obligation, based on Regulation 20 of the Civil Law Proceeding Regulations. The Company filed a motion to appeal to the Supreme Court.

In October 2005, a verdict was handed down with regard to ESHET, wherein the Supreme Court determined that class action suits are only possible by virtue of specific legislation providing for such an option, and that class action suits may not be filed for causes based on general statute by using Regulation 29 of the Civil Law Proceeding Regulations.

Consequently, the parties were required to file with the Court their position with regard to continued proceedings. The plaintiff informed the Court that it wished to continue the proceedings for causes arising from the Consumer Protection Act, which have not been approved by the District Court.

In July 2008, a settlement agreement was regarding the class action suit regarding exchange rates of passenger fees. As part of this agreement, the parties recognized the fact that the existence of two exchange rates in a single transaction would be inapplicable, and that the Company would make an effort to change regulations regarding this matter. According to the settlement, the class action against the Company shall be dismissed

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

in return for a payment of 275 thousand NIS, paid to the plaintiff's representative, which includes the entirety of expenses and legal fees of the plaintiff's representatives.

The settlement agreement is subject to the approval of the court, which is pending.

- (3) On January 22 2007, a suit was filed against the Company in the Jerusalem District Court, alongside a request to confirm the suit as a class action, to the amount of 483.4 million NIS (\$141.3 million as of the balance sheet date).

The plaintiffs claim that collecting a security surcharge to the amount of \$8 per segment from passengers on flights not carried out by the Company itself, but rather by other airlines in the framework of code sharing agreements with the Company, misleads consumers, constitutes a breach of contract, a lack of good faith and unjust enrichment, as on these flights, according to the plaintiffs' claims, security services of an equal level of those provided by the Company are provided.

The plaintiffs seek to compel the Company to pay the passengers in question a total of \$8 as well as 500 NIS as compensation for distress and inconvenience.

The Company's opinion, based on legal counsel, is that it does not expect to be found liable in this suit. No provision was made in these financial statements in respect of this claim.

b. Legal proceedings relating to overseas anti-trust proceedings

- (1) In February 2006, the Antitrust Division of the US Department of Justice ("the Antitrust Division") launched an open inquiry, along with other antitrust authorities in other countries, into allegations of price fixing with regard to certain surcharges to prices of cargo air transportation. Several air cargo transporters have announced that they had received grand jury orders with regard to this inquiry. On September 27, 2006, the Company received a grand jury order from the Antitrust Division demanding information and documents regarding pricing practices and certain surcharges related to cargo transportation, since early 1999 and through the date of said order. The Antitrust Division has informed the Company that it is under inquiry as a suspect. The Company is cooperating with the inquiry, while conducting an internal review of its cargo pricing practices. At this time, the Company is unable to estimate the outcome of the Antitrust Division inquiry, nor estimate its potential monetary impact. However, it shall be noted that implications may include administrative or civilian proceedings and/or a criminal indictment, including fines and/or civilian liability. Additionally, punishment for breach of antitrust legislation may be severe, both in terms of criminal liability and civil liability.

On May 25, 2008, the Company Board of Directors resolved to make a provision in the financial statements amounting to \$20 million (capitalized) in respect of the aforementioned Antitrust Division inquiry. This decision was made in view of a potential agreed resolution under review with the US Department of Justice, and it was made for the sake of caution, without constituting any admission of liability.

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

- (2) In December 2006, the Company received a letter from the European Commission's Directorate General for Competition ("the Directorate"), delivered to Company offices in Germany, demanding information related to an inquiry conducted by the Directorate. The letter indicates that the information requirement is in conjunction with an inquiry conducted by the Directorate with regard to activities which allegedly impact competition in air cargo transportation services, and that the Directorate has information regarding extensive communications among airlines and other entities with regard to various surcharges and other issues, such as cargo transportation tariffs.

In the letter, the Company was required to provide data and documents related to the Company and its cargo operations since 1995. The Company has provided its response as requested by the Directorate's letter, while conducting internal review of its cargo pricing practices. At this time, the Company is unable to estimate the outcome of the Directorate's inquiry, nor estimate its potential monetary impact on the Company; hence no provision was made in these financial statements with regard to the aforementioned inquiry.

According to publications by the Directorate and by several foreign companies, in December 2007 the Directorate sent a "letter of claims" to several airlines with regard to the aforementioned inquiry, including claims of alleged breach of competitive statutes of the European Union. To date, the Company has not received the aforementioned letter of claims, and to the best of its knowledge it is not among the companies to which the letter of claims was sent.

However, note that implications may include an administrative proceeding against the Company, including a substantial fine which may be imposed on the Company at the end of said proceedings.

- (3) The aforementioned proceedings related to inquiries by antitrust authorities may materially impact the Company, due to fines which said authorities may impose – which could be significant.
- (4) In late February 2007, the Company received a civilian claim filed with a New York Court, with regard to prices of cargo air transportation services.

In the aforementioned claim, to which the Company is named as defendant along with 38 other airlines, which are alleged to have colluded in coordinating prices of cargo air transportation services since 2000, in violation of competitive and other statutes in Europe and in the USA.

The claim was filed on behalf of entities purchasing cargo air transportation services, directly or indirectly, in Europe and in the USA, and includes a motion for class action status. The claim includes demand of unspecified damages and other remedies.

The Company has joined a joint defense team along with other defendant airlines, which has filed several preliminary motions with the Court, including a motion to dismiss the claim.

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

Due to the preliminary stage of this proceeding, the Company is unable to estimate its implications or monetary impact on the Company; hence no provision in respect of this claim was made in these financial statements.

- (5) In August 2008, the Company received a request from the Korea Fair Trade Commission for information pertaining to an investigation the Commission is conducting concerning possible violations of Korean competition laws in the field of air cargo shipping services, this for the period starting 1999. To the best of the Company's knowledge, the Commission is conducting its investigation in connection with several airlines. The Company has responded as requested.

c. Material legal proceedings added in the reported period

- (1) On May 29, 2008, the Company received at its head office a request to conduct an arbitration proceeding along with a claim letter (hereinafter: "the arbitration request") filed with the International Court of Arbitration of the International Chamber of Commerce in Paris by Sabre Inc. (a US-registered corporation) and by Sabre Marketing Nederland B.V. (a corporation registered in the Netherlands) with regard to the cooperation agreement signed by the Company and Sabre in 2001 (hereinafter: "the Agreement").

Pursuant to the agreement, a joint company (Sabre Israel Ltd.) was established by the Company and by Sabre Inc., engaged in providing flight reservation services and associated services.

According to the agreement, legal proceedings concerning the agreement are to be conducted in accordance with ruled of the International Court of Arbitration to be heard by a single arbitrator in London, pursuant to essential laws of Israel.

In the statement of claim, Sabre alleges that the Company is in breach of the agreement by replacing its previous reservation system with a new international reservation system. Remedies requested in the claim letter include enforcement of the agreement and provision of exclusive rights to marketing of the distribution system. Alternatively, monetary damages are claimed including, inter alia, damages amounting to \$36 million for breach of contract as well as \$67 million for impact to reputation.

Company management believes, based on legal counsel, that the aforementioned claim amount is significantly exaggerated. These financial statements include a provision in respect of this claim.

- (2) A claim was filed with the Tel Aviv District Court by a passenger, who claims that her flight from Madrid to Tel Aviv was delayed to a strike at Ben Gurion airport, which she alleges the Company has failed to address, thereby causing her expenses, distress and loss of time.

The plaintiff has filed a motion for class action status, representing all affected passengers whose flights were delayed by the aforementioned strike, estimated by the plaintiff at 3,000 passengers. The plaintiff claims that the Company should be liable to pay each class member their actual expenses as well as non-monetary damages amounting to NIS 3.500.

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

Company management believes, based on opinion of its legal counsel, that the Company is not expected to be liable for this lawsuit. These financial statements do not include a provision in respect of this claim.

Note 6 - **Taxes on revenue**

According to the Adjustment Act and to Income Tax Regulations (Rules for Accounting by Companies in Foreign Investment and Certain Partnerships and Determination of their Taxable Income), 1986 ("the USD regulations"), results for tax purposes of the Company and some of its subsidiaries are measured based on adjustment to the USD exchange rate.

The Company's major consolidated companies operating in Israel are subject to the Income Tax Act (Inflationary Adjustment), 1985 ("the Adjustment Act"), which stipulates measurement of results on a real basis, adjusted for changes in the Consumer Price Index.

On February 26, 2008, the Knesset enacted the Income Tax Act (Adjustments for inflation) (Amendment 20) (Restriction of Applicability), 2008 ("the Amendment"), whereby the Inflationary Adjustment Act's applicability would cease in 2007 and provisions of the Act would no longer apply starting in 2008, other than transition provisions aimed at avoiding tax calculation distortions.

Pursuant to the amendment, in the 2008 tax year and later, revenues would no longer be adjusted for tax purposes to a real measuring base. Furthermore, fixed asset depreciation and carry-forward tax loss amounts would no longer be linked to the CPI, such that these amounts would be adjusted for the CPI at end of the 2007 tax year, and would no longer be linked to the CPI thereafter.

The USD regulations would continue to apply to the Company after discontinuation of the Adjustment Act.

Note 7 - **Security expenses**

a. On January 27, 2008, the Israeli Government resolved as follows:

- (1) To increase the contribution by the State of Israel towards security expenses of Israeli airlines to 80% of total direct expenses in their current and future international routes (compared to the current 50% contribution).
- (2) To amend the decision by the Ministerial Committee on Social and Economic Issues, dated May 19, 2003, with regard to the Government of Israel policy with regard to scheduled airline routes. The previous decision stipulated that the Company would continue to be the Designated Carrier in all routes on which it was the designated carrier prior to publication of the Company's prospectus in 2003. The previous decision also included terms and considerations which allow the Minister of Transportation to revoke the Company's Designated Carrier status on a specific

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

route, and/or to grant rights to another Israeli Designated Carrier on a specific route, and further stipulated that the policy would be reviewed if and when total air passenger traffic to Israel, both incoming and outgoing, would exceed 10.7 million passengers annually.

The Government resolution dated January 27, 2008 stipulated that the aforementioned guideline considerations would be cancelled, and in lieu, it stipulates that the Minister of Transportation, as part of his consideration of airline policy, and subject to his statutory rights, would consider granting rights to another Designated Carrier on scheduled airline routes, and would also consider revoking the Company's Designated Carrier status on a specific route.

The Company Board of Directors has resolved to accept the aforementioned Government decision, in view of the aforementioned increase in State contribution towards security expenses of Israeli airlines and based on the declaration included in the Government decision with regard to the trend of allowing Israeli airlines to compete, in as much as possible, under fair and equitable competition with foreign airlines – while recognizing the need for a robust Israeli airline industry.

- b. As of the date of approval of these financial statements, the Government has yet to confirm a budgetary source for funding of the aforementioned increase in contribution towards security expenses, hence it has yet to provide to the Company the additional contribution (30%) towards said expenses. In these financial statements, the additional contribution by the Government of Israel towards security expenses has not been accounted for.
- c. On May 27, 2008, the Company filed a petition with the Supreme Court of Justice against the Government of Israel, the Minister of Finance, the Minister of Transportation and other respondents, due to the fact that the decision by the Government of Israel dated January 27, 2008 with regard to increased Government contribution towards the Company's security expenses, has yet to be executed.
- d. On August 24 2008, Government Resolution no. 4032 was passed on the subject of the state's participation in Israeli airline security expenses, as follows: "
 1. To revoke Government Resolution no. 3024 dated January 27 2008 (hereinafter "the Resolution") starting January 1 2009 or on the date on which the scope of passengers entering and exiting Israel by air is greater than 10.7 million passengers per year, whichever is later.
 2. Section A of the Decision shall be implemented until its cancellation as stated in Section 1 of this decision, only on flight routes for which an additional listed Israeli carrier has been actively appointed, which has started to operate on the flight route.
 3. To authorize the Ministries of Finance and Transportation and Road Safety to increase the state's participation rate in security costs for Israeli airlines, pursuant to the signing of a global aviation agreement with the EU in accordance with Government Resolution no. 441 dated September 12 2006.
 4. The budgetary expense of Government Resolution 3024, until its cancellation as denoted in Section 1, shall be financed from the Ministry of Transportation's existing budget."
- e. On September 11 2008 the Government of Israel, the Minister of Finance, the Deputy Prime Minister and the Minister of Transportation and Road Safety submitted a preliminary response to the petition ("the State's Response"). According to the State's Response, on August 24 2008 the Government

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

of Israel passed Resolution 4032 ("the Cancellation Resolution") which changes and limits the application of Government Resolution 3024 dated January 27 2008 ("the Original Resolution"), so that with the passing of the Cancellation Resolution, the basis of the petition underwent a material change and therefore the Court is requested to reject it

- f. On September 18 2008 the Company filed a request to amend the petition ("the Petition Amendment Request"), this in light of the State's response, so that is the framework of the Amended Petition, the Company shall ask the Court to issue an order to the respondents, according to which they must provide cause as to why the Cancellation Resolution should not be revoked leaving the Original Resolution - the application of which has already begun - in effect, to be applied by the Government in full, and alternately, if the Cancellation Resolution is to remain in effect, why the situation should not be returned to its previous state prior to the original resolution, including the cancellation of the appointment of other Israeli airlines as listed carriers, which was made as a result of the original resolution.

Note 8 - Operating segments

Below is information by geographic segment, on consolidated basis:

	<u>North America</u>	<u>Europe</u>	<u>Asia-Pacific and Central Asia</u>	<u>Rest of the world</u>	<u>Total</u>
	<u>USD in thousands</u>				
For the 9-month period ended September 30, 2008 (unaudited):					
Revenues -					
Segment revenues	562,431	773,101	232,171	36,824	1,604,527
Revenues not attributed to segments					31,234
Total revenues					<u>1,635,761</u>
Operating income -					
Segment operating income	11,839	109,789	22,418	5,455	149,501
Cross-segment expenses, net					(162,367)
Operating loss before financing					<u>(12,866)</u>
For the 9-month period ended					

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

September 30, 2007 (unaudited):

Revenues -					
Segment revenues	<u>500,975</u>	<u>611,846</u>	<u>240,472</u>	<u>30,070</u>	1,383,363
Revenues not attributed to segments					<u>24,793</u>
Total revenues					<u>1,408,156</u>
Operating income -					
Segment operating income	<u>44,877</u>	<u>121,479</u>	<u>19,611</u>	<u>9,882</u>	195,849
Cross-segment expenses, net					<u>(106,225)</u>
Operating income before financing					<u>89,624</u>

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

Note 8 - Operating segments (continued)

Below is information by geographic segment, on consolidated basis:

	<u>North America</u>	<u>Europe</u>	<u>Asia-Pacific and Central Asia</u>	<u>Rest of the world</u>	<u>Total</u>
	USD in thousands				
For the 3-month period ended September 30, 2008 (unaudited):					
Revenues -					
Segment revenues	<u>207,065</u>	<u>304,982</u>	<u>69,769</u>	<u>11,643</u>	593,459
Revenues not attributed to segments					<u>13,814</u>
Total revenues					<u>607,273</u>
Operating income -					
Segment operating income	<u>14,670</u>	<u>64,693</u>	<u>9,238</u>	<u>1,772</u>	90,373
Cross-segment expenses, net					<u>(39,978)</u>
Operating income before financing					<u>50,395</u>
For the 3-month period ended September 30, 2007 (unaudited):					
Revenues -					
Segment revenues	<u>204,678</u>	<u>256,741</u>	<u>85,546</u>	<u>11,071</u>	558,036
Revenues not attributed to segments					<u>8,679</u>
Total revenues					<u>566,715</u>
Operating income -					
Segment operating income	<u>27,586</u>	<u>64,761</u>	<u>8,618</u>	<u>4,035</u>	105,000
Cross-segment expenses, net					<u>(43,249)</u>
Operating income before financing					<u>61,751</u>

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

For the year ended December 31, 2007
(audited)

Revenues -

Segment revenues	<u>674,728</u>	<u>822,320</u>	<u>356,796</u>	<u>42,060</u>	1,895,904
Revenues not attributed to segments					<u>36,546</u>
Total revenues					<u>1,932,450</u>

Operating income -

Segment operating income	<u>56,662</u>	<u>144,108</u>	<u>33,405</u>	<u>11,212</u>	245,387
Cross-segment expenses, net					<u>(150,714)</u>
Operating income before financing					<u>94,673</u>

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

Note 9 - Financial information in accordance with International Financial Reporting Standards (IFRS)

a. Overview:

Following the publication of Accounting Standard no. 29 "Adoption of International Financial Reporting Standards (IFRS)" in July 2006, the Company adopted IFRS standards starting on January 01, 2008.

In accordance with provisions of IFRS 1, concerning initial adoption of IFRS, and with the date selected by the Company for initial adoption of these standards, the first financial statements to be compiled by the Group in accordance with IFRS are the consolidated financial statements as of December 31, 2008 and for the year then ended. The Company's transition date to IFRS-based reporting, as defined in IFRS 1, is January 01, 2007 (hereinafter: "the Transition Date"), with the opening balance sheet being the one as of January 01, 2007 (hereinafter: "the Opening Balance Sheet"). The Company's interim financial statements for 2008 are also compiled in accordance with IFRS, including their comparative figures.

Within the Opening Balance Sheet, the Company acted as follows:

- Recognition of any asset or liability required to be recognized on the balance sheet under IFRS.
- Non-recognition of assets or liabilities which may not be recognized on the balance sheet under IFRS.
- Classification of asset, liability and shareholder equity items as per IFRS.
- Measuring all assets and liabilities recognized under IFRS.

IFRS 1 stipulates that application of IFRS in the Opening Balance Sheet be retroactive. However, IFRS 1 sets forth several easements, for which no retroactive application is required. For the easements applied by the Company, see section (g) below.

Changes in accounting policy retroactively applied by the Company in the opening balance sheet in accordance with IFRS, compared to accounting policy based on Israeli generally accepted accounting practices have been directly recognized in retained earnings or in other items under the shareholders' equity group, as the case may be.

This Note has been compiled based on international accounting and financial reporting standards and clarifications there to as currently known, which have been published and will become effective or which may be adopted early on the Group's first annual reporting date in accordance with IFRS - December 31, 2008. As set forth in Note 1b2, Company management has made assumptions with regard to accounting policies expected to be applied when the first financial statements are compiled in accordance with IFRS for the year ending December 31, 2008.

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

IFRS standards which would be effective or which may be adopted in the financial statements for the year ending December 31, 2008 are subject to change and to further clarifications. Therefore, accounting policies applied for the reported periods would only be finally determined upon compiling the first financial statements based on IFRS, as of December 31, 2008.

Below are the consolidate balance sheets and consolidated shareholders' equity items as of January 01, 2007, September 30, 2007 and December 31, 2007 and the consolidated income statements for the 9-month and 3-month periods ended September 30, 2007 and for the year ended December 31, 2007 – compiled in accordance with IFRS. We also present the material adjustments required for transition from reporting in accordance with Israeli GAAP to reporting in accordance with IFRS.

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

Note 9 - Financial information in accordance with International Financial Reporting Standards (IFRS) (continued)**b. Consolidated Balance Sheets**

As of September 30, 2007

		<u>Israeli Standards</u>					
		As					In
Additional	Information	Previously	Effect of Re-	After Re-	Adjust-	Classifica-	accordance
		Reported	Presentation	Presentation	ments	tions	with IFRS
<u>USD in thousands</u>							
<u>Current assets</u>							
		89,143	-	89,143	-	-	89,143
		183,565	-	183,565	-	-	183,565
		171,409	-	171,409	-	-	171,409
	8	58,825	-	58,825	-	(30,450)	28,375
	3	-	-	-	8,922	1,256	10,178
	5	7,831	-	7,831	-	(7,831)	-
	8	-	-	-	-	26,845	26,845
		15,095	-	15,095	-	-	15,095
		<u>525,868</u>	<u>-</u>	<u>525,868</u>	<u>8,922</u>	<u>(10,180)</u>	<u>524,610</u>
<u>Non-current assets</u>							
		2,076	-	2,076	-	-	2,076
		2,340	-	2,340	-	-	2,340
		1,865	-	1,865	-	-	1,865
	3	-	-	-	4,987	2,349	7,336
		1,293,818	-	1,293,818	-	(307)	1,293,511
		3,626	-	3,626	-	307	3,933
		<u>1,303,725</u>	<u>-</u>	<u>1,303,725</u>	<u>4,987</u>	<u>2,349</u>	<u>1,311,061</u>
		<u>1,829,593</u>	<u>-</u>	<u>1,829,593</u>	<u>13,909</u>	<u>(7,831)</u>	<u>1,835,671</u>
<u>Current liabilities</u>							
		65,451	-	65,451	-	-	65,451
		182,653	-	182,653	-	-	182,653
	4,8	402,107	-	402,107	-	(354,213)	47,894
	2,8	-	7,436	7,436	370	79,742	87,548

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

Liabilities in respect of employee benefits	1,8	-	-	-	(2,074)	77,205	75,131
Unearned revenues	8	-	-	-	-	197,266	197,266
		650,211	7,436	657,647	(1,704)	-	655,943
<u>Non-current liabilities</u>							
Loans from banking corporations		736,191	-	736,191	-	-	736,191
Liabilities in respect of employee benefits	1	68,632	-	68,632	(17,158)	-	51,474
Long-term loans from others		473	-	473	-	-	473
Derivative financial instruments		-	-	-	225	-	225
Deferred taxes	5	61,369	-	61,369	8,444	(7,831)	61,982
		866,665	-	866,665	(8,489)	(7,831)	850,345
<u>Shareholders' equity</u>		312,717	(7,436)	305,281	24,102	-	329,383
		1,829,593	-	1,829,593	13,909	(7,831)	1,835,671

Note 9 - Financial information in accordance with International Financial Reporting Standards (IFRS) (continued)**b. Consolidated balance sheet (continued)**

	Additional Information	As of December 31, 2007				As of January 01, 2007			
		Israeli Standards	Adjustments	Classifications	In accordance with IFRS	Israeli Standards	Adjustments	Classifications	In accordance with IFRS
		USD in thousands				USD in thousands			
<u>Current assets</u>									
Cash and cash equivalents		86,670	-	-	86,670	146,158	-	-	146,158
Short-term deposits		180,633	-	-	180,633	4,682	-	-	4,682
Trade receivables		143,617	-	-	143,617	132,544	-	-	132,544
Other accounts receivable	8	51,953	-	(29,699)	22,254	47,342	-	(21,382)	25,960
Derivative financial instruments	3	-	21,881	3,649	25,530	-	5,810	-	5,810
Deferred taxes	5	19,569	592	(20,161)	-	30,645	1,368	(32,013)	-
Prepaid expenses	8	-	-	25,096	25,096	-	-	18,479	18,479
Inventory		15,981	-	-	15,981	17,190	-	-	17,190

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

Note 9 - Financial information in accordance with International Financial Reporting Standards (IFRS) (continued)**b. Consolidated balance sheet (continued)**

	<u>As of December 31, 2007</u>						<u>As of January 01, 2007</u>				
	<u>Israeli Standards</u>						<u>Israeli Standards</u>	<u>Adjustments</u>	<u>Classifications</u>	<u>In accordance with IFRS</u>	
	<u>Additional Information</u>	<u>As previously reported</u>	<u>Impact of re-statement *</u>	<u>After re-statement</u>	<u>Adjustments</u>	<u>Classifications</u>					<u>In accordance with IFRS</u>
<u>Current liabilities</u>											
Short-term credit and current maturities		66,316	-	66,316	-	-	66,316	105,100	-	-	105,100
Trade payables		167,420	-	167,420	-	-	167,420	144,990	-	-	144,990
Other accounts payable	4,8	407,842	7,435	415,277	-	(368,093)	47,185	332,691	19,930	(291,521)	61,100
Proposed dividend payable		3,008	-	3,008	-	-	3,008	-	-	-	-
Provisions	2,8	-	-	-	388	89,233	89,621	-	(138)	74,516	74,378
Derivative financial instruments	3	-	-	-	-	-	-	-	8,811	-	8,811
Liabilities in respect of employee benefits	1,8	-	-	-	(2,531)	90,109	87,578	-	(704)	74,660	73,956
Unearned revenues		-	-	-	-	188,751	188,751	-	-	142,345	142,345
		<u>644,587</u>	<u>7,435</u>	<u>652,022</u>	<u>(2,143)</u>	<u>-</u>	<u>649,879</u>	<u>582,781</u>	<u>27,900</u>	<u>-</u>	<u>610,681</u>
<u>Non-current liabilities</u>											
Loans from banking corporations		713,793	-	713,793	-	-	713,793	566,104	-	-	566,104
Liabilities in respect of employee benefits	1	70,936	-	70,936	(16,185)	-	54,751	126,171	(20,077)	-	106,094
Other long-term loans		423	-	423	-	-	423	730	-	-	730
Derivative financial instruments	3	-	-	-	2,369	(954)	1,415	-	1,861	-	1,861
Deferred taxes	5	72,510	(223)	72,287	12,450	(20,161)	64,576	74,603	6,790	(32,013)	49,380
		<u>857,662</u>	<u>(223)</u>	<u>857,439</u>	<u>(1,366)</u>	<u>(21,115)</u>	<u>834,958</u>	<u>767,608</u>	<u>(11,426)</u>	<u>(32,013)</u>	<u>724,169</u>
<u>Shareholders' equity</u>											
		<u>292,504</u>	<u>(7,212)</u>	<u>285,292</u>	<u>33,552</u>	<u>-</u>	<u>318,844</u>	<u>214,100</u>	<u>(3,038)</u>	<u>-</u>	<u>211,062</u>
		<u>1,794,753</u>	<u>-</u>	<u>1,794,753</u>	<u>30,043</u>	<u>(21,115)</u>	<u>1,803,681</u>	<u>1,564,489</u>	<u>13,436</u>	<u>(32,013)</u>	<u>1,545,913</u>

* For re-statement under Israeli standards see Note 9e.

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

Note 9 - Financial information in accordance with International Financial Reporting Standards (IFRS)
(continued)

c. Consolidated income statements

		For the 9-month period ended September 30, 2007			
		Israeli	Adjustments	Classif-	In
Additional	Information	Standards	Adjustments	ications	accordance
		USD in thousands			
		Standards	Adjustments	ications	with IFRS
		1,408,156	-	-	1,408,156
		1,110,380	(13,933)	-	1,096,447
		297,776	13,933	-	311,709
		159,365	187	-	159,552
		65,965	742	-	66,707
		-	-	(4,174)	(4,174)
		72,446	13,004	4,174	89,624
		(27,035)	(648)	(9,895)	(37,578)
		-	1,173	9,895	11,068
		45,411	13,529	4,174	63,114
		4,174	-	(4,174)	-
		49,585	13,529	-	63,114
		(9,580)	(3,555)	-	(13,135)
		40,005	9,974	-	49,979
		145	-	-	145
		40,150	9,974	-	50,124
		0.09	0.02	-	0.11
		0.08	0.02	-	0.10

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

Note 9 - Financial information in accordance with International Financial Reporting Standards (IFRS)
(continued)

c. Consolidated income statements (continued)

		For the 3-month Period Ended September 30, 2007			
Additional Information	Israeli Standards	Adjustments	Classif- ications	In accordance with IFRS	
USD in thousands					
Operating revenues		566,715	-	-	566,715
Operating expenses	1,3	415,379	(502)	-	414,877
Gross income		151,336	502	-	151,838
Selling expenses	1	65,904	63	-	65,967
General and administrative expenses	1,2	21,588	87	-	21,675
Other revenues, Net	7	-	-	2,445	2,445
Operating income before financing revenues (expenses), net		63,844	352	(2,445)	61,751
Financing expenses	3,4	(10,386)	(648)	(4,808)	(15,842)
Financing revenues	6	-	(304)	4,808	4,504
Operating income after financing revenues (expenses), net		53,458	(600)	(2,445)	50,413
Other revenues, Net	7	(2,445)	-	2,445	-
Pre-tax income		51,013	(600)	-	50,413
Taxes on revenue		(9,914)	194	-	(9,720)
Profit after taxes on revenue		41,099	(406)	-	40,693
Company share of results of investees, net		54	-	-	54
Net income for period		41,153	(406)	-	40,747
Diluted earnings per NIS 1 par value ordinary share (in USD)					
Basic earnings per share, net		0.08	-	-	0.08
Diluted earnings per share, net		0.08	-	-	0.08

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

Note 9 - Financial information in accordance with International Financial Reporting Standards (IFRS)
(continued)

c. Consolidated income statements (continued)

		For Year Ended December 31, 2007					
		Israeli Standards					
Additional Information	As previously reported	Impact of re-statement *	After re-statement	Adjustments	Classifications	In accordance with IFRS	
USD in thousands							
Operating revenues		1,932,450	-	1,932,450	-	-	1,932,450
Operating expenses	1,3	1,539,658	-	1,539,658	(21,963)	-	1,517,695
Gross income		392,792	-	392,792	21,963	-	414,755
Selling expenses	1	230,637	-	230,637	249	-	230,886
General and administrative expenses	1,2	90,781	-	90,781	838	-	91,619
Other revenues, Net	7	-	-	-	-	(2,423)	(2,423)
Operating income before financing revenues (expenses), net		71,374	-	71,374	20,876	2,423	94,673
Financing expenses	3,4	(33,393)	-	(33,393)	(5,581)	(17,088)	(56,062)
Financing revenues	6	-	(770)	(770)	3,151	17,088	19,469
Operating income after financing revenues (expenses), net		37,981	(770)	37,211	18,446	2,423	58,080
Other revenues, Net	7	2,423	-	2,423	-	(2,423)	-
Pre-tax income		40,404	(770)	39,634	18,446	-	58,080
Taxes on revenue		(9,001)	223	(8,778)	(4,808)	-	(13,586)
Profit after taxes on revenue		31,403	(547)	30,856	13,638	-	44,494
Company share of results of investees, net		332	-	332	-	-	332
Net income for period		31,735	(547)	31,188	13,638	-	44,826
Loss per NIS 1 par value ordinary share (in USD)							
Basic earnings per share, net		0.07	-	0.07	0.02	-	0.09
Diluted earnings per share, net		0.06	-	0.06	0.03	-	0.09

* For re-statement under Israeli standards see Note 9e.

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

Note 9 - Financial information in accordance with International Financial Reporting Standards (IFRS)
(continued)

d. Reconciliation to equity

	Additional Infor- mation	Share capital	Share premium	Capital reserve from transactions with former controlling shareholder	Capital reserve in respect of share- based payment	Capital reserve in respect of cash flow hedging	Accumul- ated deficit	Total
USD in thousands								
<u>As of January 01, 2007</u>								
Israeli Standards		131,536	904	218,498	2,582	-	(139,420)	214,100
Reconciliation of severance-pay liabilities, Net	1	-	-	-	-	-	15,585	15,585
Statement of hedging instruments at fair value	3	-	-	-	-	4,149	(2,945)	1,204
Statement of liabilities at fair value in respect of options issued	4	-	-	-	-	-	(19,930)	(19,930)
Statement of liabilities in respect of legal claims	2	-	-	-	-	-	103	103
In accordance with IFRS		<u>131,536</u>	<u>904</u>	<u>218,498</u>	<u>2,582</u>	<u>4,149</u>	<u>(146,607)</u>	<u>211,062</u>
<u>As of September 30, 2007</u>								
Israeli standards, as previously reported		155,012	9,248	243,787	3,940	-	(99,270)	312,717
Impact of re-statement *		-	-	(7,436)	-	-	-	(7,436)
Israeli standards, after re-statement		155,012	9,248	236,351	3,940	-	(99,270)	305,281
Reconciliation of severance-pay liabilities, Net	1	-	-	-	-	-	14,424	14,424
Statement of hedging instruments at fair value	3	-	-	-	-	2,556	7,399	9,955
Statement of liabilities at fair value in respect of options issued	4	-	18,759	-	-	-	(18,759)	-
Statement of liabilities in respect of legal claims	2	-	-	-	-	-	(278)	(278)
In accordance with IFRS		<u>155,012</u>	<u>28,007</u>	<u>236,351</u>	<u>3,940</u>	<u>2,556</u>	<u>(96,483)</u>	<u>329,383</u>
<u>As of December 31, 2007</u>								
Israeli standards, as previously reported		155,012	9,248	243,787	4,464	-	(120,007)	292,504
Impact of re-statement *		-	-	(6,665)	-	-	(547)	(7,212)
Israeli standards, after re-statement		155,012	9,248	237,122	4,464	-	(120,554)	285,292
Reconciliation of severance-pay liabilities, Net	1	-	-	-	-	-	14,037	14,037
Statement of hedging instruments at fair value	3	-	-	-	-	8,341	11,464	19,805
Statement of liabilities at fair value in respect of options issued	4	-	18,759	-	-	-	(18,759)	-
Statement of liabilities in respect of legal claims	2	-	-	-	-	-	(290)	(290)
In accordance with IFRS		<u>155,012</u>	<u>28,007</u>	<u>237,122</u>	<u>4,464</u>	<u>8,341</u>	<u>(114,102)</u>	<u>318,844</u>

* For re-statement under Israeli standards see Note 9e.

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

Note 9 - Financial information in accordance with International Financial Reporting Standards (IFRS)
(continued)

- e. The financial statements as of December 31, 2007 and for the year then ended have been restated (in conjunction with Israeli standards), such that the capital reserve from transactions with an ex-controlling shareholder was reduced by \$6,665 thousand, against recording of a liability, pending clarification of the status of excess proceeds from option exercise deposited by the State in the employee severance pay fund beyond the "deficit" in the employee severance pay fund - as defined in the agreement signed on June 3, 2003 by the Company, the State and employee representatives. The impact on financing revenues for the year ended December 31, 2007 is a decrease of \$770 thousand, as well as a decrease of \$223 thousand in tax expenses.

f. Additional Information

- (1) Under Israeli GAAP, severance pay liabilities are recognized based on the full liability, assuming that all employees are terminated upon the balance sheet date under circumstances entitling them to receive full severance pay, regardless of discount rate, any future pay increase rate and future departures. In accordance with IFRS, all liabilities in respect of post-retirement benefits to employees and other long-term benefit plans are measured in accordance with provisions of IAS 19 "Employee benefits". Employee benefits which constitute defined benefit plans are measured, *inter alia*, based on actuarial estimates and discounted amounts. Furthermore, in accordance with IFRS, no severance pay provision is recorded in cases where the employee benefit would only be granted upon termination by the employer.

Provision for early retirement programs – in accordance with Israeli GAAP, provisions for early retirement programs are made in accordance with management expectations with regard to their realization. In accordance with IFRS, retirement programs are only recognized when a formal, detailed retirement program is in place which creates an irrevocable commitment on behalf of the Company.

Furthermore, in accordance with Israeli GAAP, a provision for paid leave is recognized based on the full liability, assuming that employees would utilize all their paid leave in the short term.

In accordance with IFRS, provisions for paid leave are made in accordance with expected paid leave utilization, and are measured based on actuarial estimates and capitalized amounts.

To date, the Company has recorded a provision for redemption of unutilized sick pay upon retirement, only for employees who have reached the age of 45 and using non-capitalized amounts. In accordance with IFRS, this provision was calculated in respect of all Company employees, based on actuarial estimates and using capitalized amounts.

The impact of the above on the balance sheet is a decrease in liabilities for employee benefit programs, net as of January 01, 2007, September 30, 2007 and December 31, 2007 amounting to \$20,781 thousand, \$19,232 thousand and \$18,716 thousand, respectively.

Furthermore, deferred taxes receivable as of January 01, 2007, September 30, 2007 and December 31, 2007 were decreased by \$5,196 thousand, \$4,808 thousand and \$4,679 thousand, respectively.

The discount rate used for calculation of actuarial liabilities was determined using market returns of government bonds, since the Company believes there is no deep market of high-quality corporate bonds in Israel. The issue of the discount rate is under review, which may result in a decision that the appropriate discount rate in Israel is based on market returns of corporate bonds. Should such a decision be made, the calculated data presented in the Notes would change, since use of a higher discount rate would reduce

EL AL Israel Airlines Ltd.

Notes to condensed consolidated financial statements

actuarial liabilities and would increase the current interest cost in respect of actuarial liabilities.

- (2) According to Israeli GAAP, the Company recognizes a provision for contingent claims if use of economic resources to discharge the liability is probable. Under IFRS, a provision should be recognized if a liability is more likely than not to exist as of the balance sheet date. The provision under IFRS is determined by the amount which the Company estimates it would be willing to pay in order to settle the claim.

Therefore the following changes were made to the provision for legal claims as of January 01, 2007, September 30, 2007 and December 31, 2007: A decrease of \$138 thousand, an increase of \$370 thousand and an increase of \$388 thousand, respectively. Furthermore, the following changes were made to deferred tax liabilities as of January 01, 2007, September 30, 2007 and December 31, 2007: An increase of \$35 thousand, a decrease of \$93 thousand and a decrease of \$98 thousand, respectively.

- (3) Unlike Israeli GAAP, under IAS 39 all derivative financial instruments are recognized as assets or liabilities at their fair value. Changes to fair value would be recognized in the income statements (for instruments which do not meet the required conditions to be recognized as hedges) or in a capital reserve (for instruments designated as cash flow hedges which meet the required conditions to be recognized as hedges). Upon transition to IFRS, some of the jet fuel hedging transactions and some of the interest rate hedging transactions, designated by Company management as hedges, will be stated in the opening balance sheet at fair value, against a capital reserve. The change in fair value of these hedging transactions in subsequent periods will be charged to a capital reserve, for the effective portion of the hedging instrument, and to operating expenses or to financing expenses, as the case may be, in the income statement, for the non-effective portion.

Company management has decided that under IFRS, foreign currency hedging transactions and some jet fuel and interest rate hedging transactions will be treated as if not designated as hedges, therefore any change in fair value of said transactions in subsequent periods will be recognized under fuel expenses or financing expenses in the income statement, as the case may be.

Due to statement of fair value of all hedging instruments, as of January 01, 2007, September 30, 2007 and December 31, 2007, changes were made to financial and other asset items as well as to financial and other liability items included under current assets, non-current assets, current liabilities and non-current liabilities amounting to a net total of \$1,396 thousand, \$13,909 thousand and \$27,082 thousand, respectively.

Concurrently, a reserve for deferred taxes was recorded as of January 01, 2007, September 30, 2007 and December 31, 2007.

Furthermore, in respect of hedging transactions designated as hedges, a capital reserve was recorded as of January 01, 2007, September 30, 2007 and December 31, 2007 amounting to \$4,149 thousand, \$2,556 thousand and \$8,341 thousand, respectively.

- (4) Option warrants (Series 1) previously issued by the Company, the exercise price of which is linked to the CPI and is not denominated in the Company's functional currency, constitute a financial liability since they have an adjustable exercise price. In accordance with provisions of IAS 32, the liability in respect of the aforementioned option warrants should be recorded in the opening balance sheet under other accounts payable (since their exercise date was in 2007) at fair value. Changes to fair value in subsequent periods were recognized under financing in the income statement for each period. Upon exercise of said option warrants, the aforementioned liability is added to the premium, such that shares resulting from exercise of these options are recorded at fair value.

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

As a result, the derivative financial instruments item under current liabilities (against decrease in retained earnings) as of January 01, 2007 increased by \$19,930 thousand.

The aforementioned option warrants have been exercised by June 2007.

- (5) In accordance with Israeli GAAP, assets and reserves in respect of deferred taxes have been classified as current or non-current assets, or as current or non-current liabilities, based on classification of the assets and/or liabilities for which they have been created.

In accordance with IAS 1, assets and reserves in respect of deferred taxes are classified as a net, non-current asset or a reserve (as the case may be) even if their expected utilization date is within the short term.

Therefore, as of January 01, 2007, September 30, 2007 and December 31, 2007 amounts of \$32,013 thousand, \$7,831 thousand and \$20,161 thousand, respectively, were re-classified from deferred taxes receivable under current assets to deferred taxes under non-current liabilities.

- (6) According to Israeli GAAP, financing expenses and revenues are presented in the income statement as a single amount. In accordance with IFRS, financing expenses and revenues are to be presented separately.

As a result, for the 9-month and 3-month periods ended September 30, 2007 and for 2007, financing revenues amounting to \$11,714 thousand, \$4,738 thousand and \$19,469 thousand, respectively, have been presented separately.

- (7) In accordance with IFRS, other revenues and expenses would no longer be included as a separate item after financing revenues and expenses, as was the case under Israeli standards, but would be included under operating income. As a result, for the 9-month and 3-month periods ended September 30, 2007 and for 2007, other revenues (losses), net amounting to \$4,174 thousand, (\$2,445) thousand and \$2,423 thousand, respectively, were re-classified under operating income.

- (8) In accordance with IFRS, items which are not financial instruments under current assets were re-classified from other accounts receivable and were separately presented on the balance sheet.

Furthermore, under current liabilities, non-financial liabilities – unearned revenues were re-classified from other accounts payable. Furthermore, provisions and employee benefits were separately classified.

Derivative financial instruments were presented under a separate item of current assets, non-current assets, current liabilities and non-current liabilities, as the case may be.

g. Easements with regard to retroactive application of IFRS standards adopted by the Company

IFRS 1 sets forth several easements, for which no retroactive application is required. The Company has elected to apply the following easements to its opening balance sheet in accordance with IFRS as of January 1, 2007 ("the opening balance sheet").

- (1) Employee benefits -

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

The Company applies the corridor approach to recognition of actuarial gains and losses, as per provisions of IAS 19. The Company has elected to recognize all actuarial gains and losses accumulated through January 1, 2007 under retained earnings.

(2) Hedge accounting -

Some interest hedging transactions, which constitute cash flow hedges and which meet hedging requirements of IAS 39, but do not meet specific designation and documentation requirements, were classified upon the transition date as hedging transactions. This is due to the fact that the Company has completed specific designation and documentation of said instruments' hedging ratios by the transition date.

Note 10 - Events subsequent to the balance sheet date

- a. On November 2 2008 a collective agreement was signed by the Company, the employees' representatives and the Histadrut ("the Agreement") following the Board of Director's approval of the Agreement on October 27 2008. The primary points of this agreement are as follows:
- The Agreement shall be in effect until December 31 2012.
 - Industrial peace and discipline - a commitment exists to uphold industrial peace for the duration of the agreement, while focusing on competition and growth challenges. The Company, the Histadrut and the employees' representatives shall conduct joint activities to promote and maintain order and discipline in the Company. The Company's authority as regards the termination of employees guilty of severe disciplinary violations shall be expanded.
 - Bonuses and pay raises – when the Company becomes profitable, a general pay raise shall be granted equal to 3% of their pension salaries. In the event of profits greater than \$10 million, employee shall receive a one-time bonus equal to between 18% and 24% of their base salaries. In addition, in the following year, if the Company earns over \$10 million, an addition raise equal to 1% of pension salaries shall be granted. If the Company earns over \$35 million, an additional 0.5% shall be added to salaries. In the following year, if the Company earns over \$10 million, an additional 1% shall be added to pension salaries. If the Company earns over \$35 million an additional 0.5% shall be added.
 - Horizon promotion bonus – when the Company becomes profitable, an annual budget for the financing of a horizon promotion bonus for non-promoted ground personnel as well as for flight crews and flight attendants with similar status. Non-promoted employees are workers who have spend many years at the top step of the existing standard pay scale and are not designated for promotion.
 - Work cessation – initiated retirement and/or work cessation of 30 employees via a process including work cessation pathways using an increased compensation format, early pension or a choice between the above (in accordance with the retiring worker's age).
 - Shifts and rest periods – shifts in Israel station and maintenance shall be adjusted and reinforced according to activity loads. Rest periods for pilots and regular and temporary flight attendants in North America shall be shortened.
 - Special tracks and promotion – temporary employees with more than 3 years seniority may participate in bids for entry-level managerial positions. The Company shall be permitted to employ up to 40 employees via personal contracts. Employees in the flight technical files shall receive tenure after their fourth year instead of their second.

EL AL Israel Airlines Ltd.
Notes to condensed consolidated financial statements

- b. In October 2008 the Company signed a code share agreement with Belavia-Belarusian Airlines (hereinafter: "**Belavia**"). According to the agreement, which is a "soft block" type agreement, El Al shall receive a seat allotment on flights operated by Belavia, which shall operate between 2 and 5 weekly flights on the Tel Aviv-Minsk line, based on the seasonality of traffic. The flights shall operate in an economy class-only configuration. This agreement shall go into effect on November 30 2008, subject to approval by Israeli and Belarusian authorities.
- c. On October 2, 2008, the Chairman of the Company's Board of Directors, Dr. Israel (Izzy) Borowitz announced that he would be resigning his position as Chairman of the Board, starting November 30 2008 (Dr. Borowitz will continue to serve on the Board of Directors).

The Company also reported that the following had been decided in the meeting of the Board of Directors held on that date:

- (a) To appoint Mr. Amnon Lipkin-Shahak, a Company director, to the post of Temporary Chairman of the Board starting December 1 2008 until a permanent Chairman is appointed;
- (b) To appoint Mr. Yehuda (Yudi) Levi, a Company director, to the post of Vice Chairman of the Company's Board of Directors (in addition to Ms. Tamar Moses, serving as Vice Chairperson);
- (c) To act to appoint Mr. Amikam Cohen as a director on the Board.

On November 19 2008 the Company shareholders' general meeting confirmed the appointment of Dr. Yehoshua (Shuki) Shemer as an outside director.

- d. Towards the end of the third quarter and in the period since, jet fuel prices have continued to drop, dollar interest rates have decreased and the shekel has been devaluated relative to the dollar.

As of the balance sheet date (September 30 2008), the jet fuel price in the Mediterranean Basin Market was 284.0 cents per gallon. Following the balance sheet date, jet fuel prices dropped significantly and immediately prior to the approval of the quarter 3 2008 report (November 16 2008), the price is 184.4 cents per gallon.

Following the drop in jet fuel prices the Company, as required by agreements with hedging institution, provided interest-bearing guarantees to the amount of \$8 million for jet fuel hedging agreements open as of the financial statement date to the hedging institutions. This trend continued after the balance sheet date, and the Company provided additional guarantees, as required. Note that the scopes of the guarantees change from day to day in accordance with jets fuel market prices and the Company makes daily calculations regarding changes needed to guarantees and their scope. The Company is negotiating with several banks for their provision of lines of credit for the issue of letters of credit for the Company for the aforementioned hedging agreements in return for liens on assets, this in lieu of deposits. The assets the Company intends to place liens on in return for these credit lines are aircraft owned by the Company that are free of liens. As of these financial statements, the negotiations have yet to develop into an agreement with the banks. The Company estimates that appropriate solutions will be found to for the release of deposits provided as guarantees for hedging institutions.

Between the balance sheet date (September 30 2008) and a date immediately prior to the confirmation of the quarter 3 2008 report (November 16 2008), three-month LIBOR interest rates decreased by a rate of 45%.

The impact of the drop in LIBOR interest rates has on loan interest payments shall be expressed in the each loans next repayment date, meaning 2009 and onward. Interest repayments for Company loans for the fourth quarter of 2008 shall be made according to interest rates existing in previous quarters. The Company has defense agreements for LIBOR rates, the fair value of which is expected to drop following the drop in LIBOR interest rates.

EL AL Israel Airlines Ltd.

Notes to condensed consolidated financial statements

Between the balance sheet date (September 30 2008) and a date immediately prior to the confirmation of the quarter 3 2008 report (November 16 2008), the shekel was devaluated by 0.46 NIS relative to the USD. The projected impact this devaluation will have as regards October 2008 is a \$2 million reduction of cash flow expenses compared to September 2008. Nevertheless, the Company has dollar rate defense agreements, the fair value of which is expected to drop as a result of the shekel's devaluation relative to the dollar.

In addition to the above, the shekel's devaluation in relation to the dollar reduces the Company's shekel liabilities in dollar terms, thus reducing the Company's salary and financing expenses.

Note that the impact exchange rates will have on next quarter's business results shall be determined based on exchange rates in effect throughout the quarter in its entirety and at its end (December 31, 2008).