

EL AL ISRAEL AIRLINES LTD.

FINANCIAL STATEMENTS

AS OF JUNE 30, 2007

(unaudited)

CONTENTS

SECTION A - UPDATE OF CHAPTER A TO 2006 ANNUAL REPORT

SECTION B - DIRECTORS' REPORT

SECTION C - FINANCIAL STATEMENTS

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

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

To item 3.2 – options

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

By June 5, 2007, 99,998,588 options (Series 1) of 100,000,000 options were exercised. The balance of options (Series 1) not yet exercised by June 5, 2007 (1,412 options) expired and are null and void.

As at June 30, 2007, the total options allotted under the Company's 2006 option plan for employees and officers, net of the options that returned to the reserve for whatever reason, based on the terms of the plan, stand at 16,977,685 options.

To Item 3.4 and 3.5 – changes in interested party holdings

On June 5, 2007, the State of Israel ceased being an interested party in the Company, and as at June 30, 2007, the State holds 1.13% of the Company's issued capital on an undiluted basis and 1.10% on a fully diluted basis, in addition to the special State share (see Par. 9.11.9 of the Periodic Report).

Presented below are the updated holdings of interested parties as at June 30, 2007, after the exercise of the call options (Series B) and exercise of options (Series 1) as provided above:

Knafaim Holdings Ltd. holds 39.33% of the Company's issued capital on an undiluted basis and 38.02% on a fully diluted basis;

Pinchas Ginsburg holds 7.69% of the issued capital on an undiluted basis and 7.43% on a fully diluted basis;

El Al Employees Corporation holds 6.56% of issued capital on an undiluted basis and 6.34% on a fully diluted basis;

Tamar Borovitz, Deputy Chairman of the Company, directly holds 0.01% of the issued capital.

The calculation of the percentage of holdings in capital and voting rights on a fully diluted basis assumes the exercise of all the options pursuant to the Company's 2006 option plan for employees and officers.

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

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

In the quarter ended June 30, 2007, market prices of jet fuel decreased by an average of 3%, compared with the same quarter last year. The Company's jet fuel expenses increased by 11%, after hedging repayments, compared with the same quarter last year. However, the Company's fuel expenses fell from 27.2% of turnover in the second quarter of 2006 to 26.5% in the reported period.

To Item 6.4 – Fluctuations in inter-currency exchange rates

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

As of June 30, 2007, there was a 4.3% decrease in the exchange rate of the U.S. dollar against the shekel compared with June 30, 2006, an increase of 2.3% compared with March 31, 2007 and an increase of 0.6% compared with December 31, 2006.

As of June 30, 2007, there was a 5.1% increase in the exchange rate of the U.S. dollar against the euro compared with June 30, 2006, an increase of 0.9% compared with March 31, 2007 and an increase of 2.0% compared with December 31, 2006.

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

To Item 6.5 – Fluctuations in interest rates

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

In the second quarter of 2007, the 3-month Libor interest rate increased by an average of 2.6%, compared with its average rate in the second quarter of 2006, and remained at the same average rate as in the quarter ended March 31, 2007.

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

2. Passenger Aircraft Area

To Item 6.2 – Traffic in the Israel aviation industry and to Item 7.1.3(B) Developments in the volume of activity in the Israeli market

According to the data of the Central Bureau of Statistics, in the months April-June 2007 there was a decrease of 10.5% in the number of inbound tourists traveling to Israel by air, compared with the same quarter last year, and an increase of 4.5% in the number of outbound Israelis traveling by air, compared with the same quarter last year. In total, the traffic in Ben-Gurion Airport grew by 4% compared with the same quarter last year.

To Item 7.1.4 – Developments in the markets of the areas of activity, Item 7.1.10(E) – Competitive structure in areas of activity and changes therein – Low Cost companies – Item 9.11.7.2 – Designated carrier and Item 9.18.12 – Discussion of risk factors: Effect of activity of Low Cost companies on the Israeli market

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

- A) The British company, "Thomsonfly", a low cost company of the TUI Group, announced its intention, beginning in the upcoming winter season, to commence operation of 3 scheduled weekly flights on the Luton (western London) – Tel Aviv route and 3 scheduled weekly flights on the Manchester – Tel Aviv route.
- B) According to newspaper reports, two other low cost companies from the TUI Group could begin operating scheduled flights to Israel - the French company Corsair on the Paris – Tel Aviv route and the Belgian company Jetair on the Liège – Tel Aviv route.
- C) According to newspaper reports, Thomson and Jetair will be given a financial "safety net" by the Ministry of Tourism and the State of Israel, according to agreements reached with these entities.

It should be noted that until the publication date of this report, the Company did not receive official notice from the Ministry of Transportation on the granting of approval to these companies. Additionally, according to newspaper reports, since these companies are subsidiaries of the German company TUI, a question could arise as to ownership and control of capital and the possibility of appointing them a "designated carrier" for the countries of England, France and Belgium (see Item 9.11.7.3 of the Immediate Report). Accordingly, at this stage, it is not possible to estimate whether these developments will occur and what their effect on the Company will be.

To Item 7.1.5 – Technological changes

Further to the details of Item 7.1.5 of the Immediate Report, it should be noted that the "Rotem" System (a system for planning air crew staffing) was integrated and is operating in the Company.

To Items 7.1.4 – Developments in the markets, Item 7.1.8 – Main entry and exit barriers of the area of activity and changes therein, 7.1.10 – Structure of competition in area of activity and changes therein, 9.11.7.4 – Capacity, 9.11.7 – Aviation agreements and Israel's civil and international aviation policy, 9.18.3 – Discussion of risk factors: changes in competition

- A) Further to the information provided in the aforementioned Items in the Immediate Report and in the update of these Items, as provided in the financial statements as at March 31, 2007, it should be noted that as far as the Company knows, at the end of July 2007, contacts were initiated for negotiations between the State of Israel and the European Union Commission regarding a new

uniform global aviation agreement opposite the EU member countries, to replace the bilateral agreements now existing between Israel and the various countries of the EU.

- B) Further to the information provided in the aforementioned Items of the Immediate Report and in the update of these Items, as provided in the financial statements as at March 31, 2007, it should be noted that in aviation discussions held between Israel and Thailand, it was agreed that the designated carriers would be allowed to operate flights between any point in Israel and any point in Thailand, including the possibility of combining two destinations in the second country on the same flight, without limit as to frequency, capacity or type of aircraft. Also agreed was the possibility of preparing "code share" agreements between the carriers from the two countries.

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

In the second quarter of 2007, an increase of 17% was posted in the foreign charter traffic in BGA compared with the same quarter last year, due mainly to the discontinuation of the activities of the Company and of the Israeli charter companies on the Turkish routes, against the backdrop of the high security costs borne by the Israeli companies.

To Item 7.2(C) – Routes to North America (U.S. and Canada)

In the second quarter of 2007, there was a decrease of 5% in passenger traffic on the transatlantic routes, compared with the same quarter last year. However, it is not possible to estimate the implications of this data on the annual change in these routes.

To Item 7.2(F) – Other routes

In the "Other Routes" (Turkey, Greece, Cyprus, South Africa and Egypt), there was growth of 11% in passenger traffic compared with the same quarter last year. However, it is not possible to estimate the implications of this data on the annual change in these routes.

As a result of the discontinuation of flights to destinations in Turkey by Israeli airlines because of the high security costs, there was a 28% increase in the activity of Turkish Airlines to Israel and a 42% increase in the activity of Turkish charter companies.

To Item 7.4 – New services

In July 2007, the Company signed an agreement with Israir Airlines and Tourism Ltd., whereby full maintenance services will be provided for Airbus A-320 aircraft. It should be noted that the agreement's taking effect is contingent on the fulfillment of several pre-conditions. To date, the Company has sold maintenance services only for Boeing aircraft. Receipt of a license for El Al's Bedek Institute for A-320 aircraft is expected to expand the maintenance services that the Company is able to sell to other airlines.

To Item 7.11 – Passenger aircraft fleet

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

- A) At the end of July 2007, the Company received possession of one of two new Boeing 777-200 ER aircraft that it had purchased from Boeing. In the Group's service, the aircraft will contain 279 seats, including bed-seats (that can recline to a prone or almost prone position) in the premium classes as well as new entertainment systems and a new design.
- B) In June 2007, the Company signed a letter of intent to lease two 737-800 aircrafts – one beginning in August 2008 and the second in October 2008, for a lease period of 8 years,

with an option to purchase one of the aircraft at the end of the lease period. The aircraft are new – from the production line, and in the Company's service will each contain 142 seats.

- C) Further to the information in Item 7.11(C), it should be noted that in April 2007, the Company signed an agreement for the purchase of bed-seats (seats that can recline to a prone or almost prone position) in the premium classes of the 747-700 and 777 aircraft. Two of the 777 aircraft that were purchased from Boeing will be delivered to the Company with the new seats already installed. In total, pursuant to the said agreement, bed-seats were ordered for ten aircraft.
- D) The Company initiated contact to explore the possibility of purchasing and/or leasing Boeing 787 model plane beginning from 2011.

3. Cargo aircraft segment

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

According to IATA reports, in the months January – June 2007 there was an increase of just 2.7% in the volume of global transport of cargo in cargo planes compared with the same period in 2006 – i.e. growth at a lower rate than the annual rate projected by IATA (5.3%). The halt in the growth was due to the high fuel prices and competition from alternative means of transportation, especially shipping by sea. Nonetheless, it is not possible to estimate whether this data changes expectations regarding the total annual growth rate for 2007.

To Item 8.2 – Services in the area of activity

Further to the information provided in Item 8.2 to the Immediate Report related to the agreement with Agrexco, it should be noted that according to understandings between the Company and Agrexco, the undertaking was extended for one additional year, as from November 30, 2007.

To Item 8.7.1E – Competitive conditions in the area of activity

Further to the information provided in Item 8.7.1E and at the end of Item 8.2 of the Periodic Report, it should be noted that the Group estimates that its share in cargo transport in the first half of 2007, out of the total cargo transported by air to and from Israel (including cargo transported in the underbelly of passenger planes, including mail and excluding sixth freedom) stood at 37.6%.

4. Information on the two operating segments

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

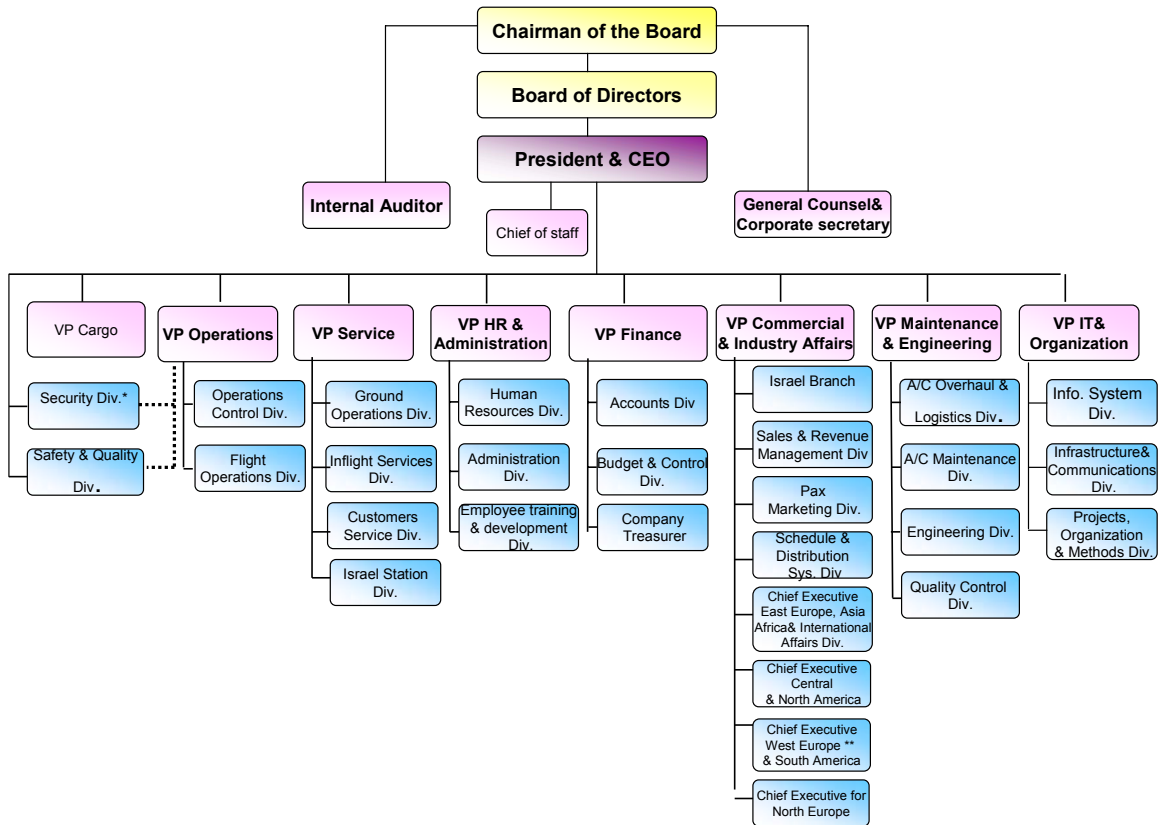
Further to the information in the aforementioned Items of the Periodic Report, and the updates to these Items, as provided in the financial statements as of March 31, 2007:

- 1) In August 2007, it was decided to place the cargo division under the responsibility of a vice-president, and a VP Cargo was appointed.
- 2) In August 2007, a chief of staff was added to the Company's executive management.

Translation of the Hebrew Language financial statements

As a result of the above organizational changes, the number of members of executive management mentioned in the table in Item 9.4.16 of the Periodic Report was updated to 11 (excluding the Chief Executive Officer) and the number of expanded management and other senior employees was updated in that table to 29.

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



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

To Item 9.4.7 – Special collective agreements

Further to the information provided in Item 9.4.7 of the Periodic Report, and the update as provided in the financial statements as at March 31, 2007, and as reported by the Company in the Immediate Report dated July 1, 2007, on June 28, 2007, notice was received in the Company's offices from the Histadrut – the union division ("the Histadrut"), by virtue of the Labor Disputes Resolution Law, 1957, whereby the Histadrut was given the right to declare a strike commencing July 18, 2007.

According to the wording of the notice, the dispute relates to the Company's management intention to evaluate the possibility of worsening the terms of the existing collective agreement and even cancel it, for reasons including the resolution by the Company's board of directors from April 18, 2007, which empowered the Company's management to take all measures necessary, including a decision to cancel the collective agreement and implementing efficiency measures.

The Company's management rejected the claims of the Histadrut and even clarified to the Histadrut that it does not intend, at this stage, to cancel the collective agreement and that there is no cause for declaring the dispute. The Company's management called on the Histadrut and the employee representatives to cancel the notice and return to negotiations, in order to continue proper work relations. Until the approval date of this Report, no actions were taken by the Histadrut and the negotiations are continuing.

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

As a result of the exercise of the options described previously in the update to Item 3.2, from January 1, 2007 through July 22, 2007, deposits were made in the severance pay fund of eligible employees: deposits by the State totaling NIS 104,624,444, and deposits by the Company totaling NIS 92,956,561. In total deposits of NIS 197,581,005 were made in the severance pay funds of eligible employees during the said period.

To Item 9.4.11 – Mutually agreed early retirement plan for employees

- A) During the second quarter of 2007, 20 employees took early Voluntary retirement, guaranteed by the Company.
- B) On August 15, 2007, the Company's board of directors approved implementation of the mutually agreed early retirement plan in 2007, for 60 employees. Accordingly, during the reported period, an appropriate provision was recorded in the financial statements. For additional information, see Note 6.4 to the financial statements.

To Item 9.4.13 – Israeli employees stationed overseas

Within the scope of the efficiency measures adopted by the Company, the number of employees stationed abroad was reduced from 34 as at December 31, 2006 to 26 as at June 30, 2007.

To Item 9.5.2 – Raw materials and suppliers: aircrafts

As reported by the Company in the Immediate Report dated July 3, 2007, the clarification signed with Boeing regarding an overall accounting between the parties included consent, whereby the sum of \$6.5 million of the cash flows received and/or expected to be received from Boeing constitutes damages for loss of revenues sustained by the Company due to the discontinuation of two joint projects, including the broadband Internet project (see Par. 7.1.5 of the Periodic Report).

The above sum was expressed in the financial statement for the reported quarter, in the item "other income" of the Company – see Note 6.3.

To Item 9.6.5 – Working capital deficit

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

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

Further to the information in Par. 9.8.4 in the Periodic Report pertaining to the guarantee of the U.S. Export-Import Bank (Ex-Im) regarding the purchase of two Boeing 777 aircrafts, it should be noted that the final commitment from Ex-Im was received on July 12, 2007 and will serve as collateral for the financing banks. During July 2007, a financing agreement with the financing banks was also signed.

For the first plane, which was delivered to the Company in July 2007, the Company received a loan of \$109 million, with \$88 million earmarked for the payment of the unpaid balance of the aircraft to Boeing and expenses related to the raising of capital. The balance of \$21 million was returned to the Company. For additional information on the purchase of the two Boeing 777 aircrafts, see Par. 7.11(A) of the Periodic Report and its update, and Note 8.1 to the financial statements.

To Item 9.8.3 – Credit facilities

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

To Item 9.10.3 – Airport noise regulations

Further to the information in Item 9.10.3 of the Periodic Report, regarding the discussion on imposing operating limitations on noise-producing planes in the Amsterdam Airport, it should be noted that the Company received notice of changes in the rates charged planes in the category to which the cargo planes operated by the Company are classified, commencing November 2007. The Company estimates that the changes included in this notice will not have a material effect on the operation of the Company's cargo planes.

The Company's estimate is forward-looking information as defined in the Israeli Securities Law, 1968, which is based on information held by the Company at the date of this Report, supported by the notice of the Schiphol Airport Authority in Amsterdam and the existing operating costs of the cargo planes, and changes in the actual data could change the estimate.

To Item 9.14 – Legal proceedings

- A) Further to the information in Item 9.14.7 of the Periodic Report, it should be noted that the court ordered the plaintiffs to quantify their claim and to pay a fee accordingly. The plaintiffs quantified the claim at NIS 18,055,897 (\$4.25 million).
- B) Further to the information in Item 9.14.8 of the Periodic Report, it should be noted that the Company sent to the Anti-Trust Commission the information required according to the order.
- C) Further to the information in Item 9.14.10 of the Periodic Report, it should be noted that the Company joined the joint defense team comprised of other airlines being sued, within the scope of which several preliminary motions have been filed with the court, including a motion to dismiss the claim or parts thereof.

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

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

El Al Israel Airlines Ltd. ("The Company") closed the three months ended June 30, 2007 with net income of \$12.6 million, compared with a loss of \$10.4 million in the same period last year.

The Company's sales turnover in the second quarter of the year increased by 5.5% over the same quarter last year, totaling \$453 million.

Gross profit in the second quarter of the year totaled \$98.9 million, 22% of turnover, whereas in the same quarter last year, it totaled \$66.4 million, 15% of turnover.

Net cash provided by operating activities in the second quarter of the year totaled \$72.1 million, and the balance of cash and short-term investments as at June 30, 2007 totaled \$232.1 million.

Shareholders' equity as at June 30, 2007 totaled \$256.9 million, compared with \$214.1 million as at December 31, 2006.

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

1. The Company and its business environment

1.1 General

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

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

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

The Group has two operating segments:

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

1.2 Privatization of the Company

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

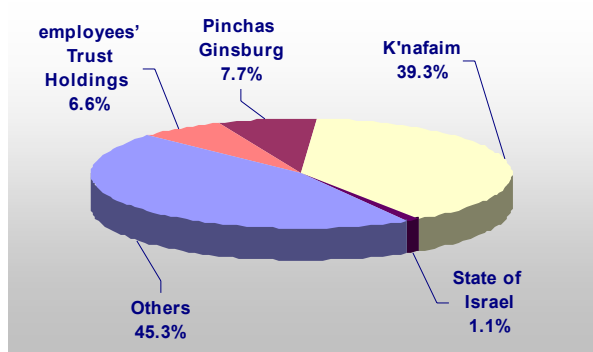
Additionally, by June 5, 2007, 99,998,588 options (Series 1) out of 100,000,000 options were exercised. The balance of unexercised options (Series 1) as at June 5, 2007 (1,412 options) expired, and are null and void.

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

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

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

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



2. Financial position (consolidated financial statements)

	30.06.2007	31.12.2006 *	Change	
	In thousands of dollars	In thousands of dollars	In thousands of dollars	%
Assets				
Cash and short-term investments	232,075	150,840	81,235	54%
Trade accounts receivable	189,547	132,544	57,003	43%
Receivables	61,279	47,342	13,937	29%
Deferred income taxes	22,041	30,645	(8,604)	(28%)
Inventory	19,331	17,190	2,141	12%
Investments	6,153	5,945	208	3%
Fixed assets	1,144,268	1,176,528	(32,260)	(3%)
Other assets	3,364	3,455	(91)	(3%)
	1,678,058	1,564,489	113,569	7%
Liabilities & Equity				
Short-term borrowings and current maturities	101,873	105,100	(3,227)	(3%)
Trade accounts payable	161,248	144,990	16,258	11%
Payables and other current liabilities	457,730	332,691	125,039	38%
Long-term loans from financial institutions	548,816	566,104	(17,288)	(3%)
Accrued severance pay, net	85,283	126,171	(40,888)	(32%)
Deferred income taxes	65,635	74,603	(8,968)	(12%)
Other long-term liabilities	563	730	(167)	(23%)
Shareholders' equity	256,910	214,100	42,810	20%
	1,678,058	1,564,489	113,569	7%

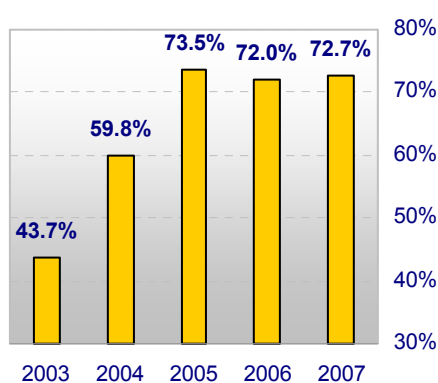
* Restated – see Note 1.3.1 and Note 1.5 to the interim financial statements.

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

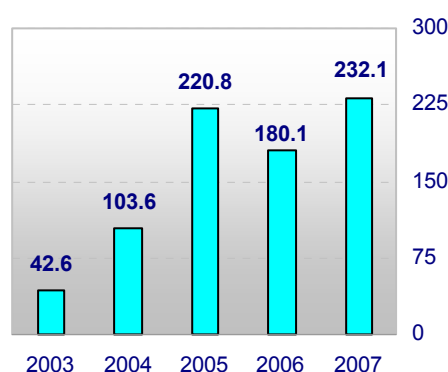
- Increase in cash and short-term investments, due mainly to the positive cash flows from operating activities in the current period, offset by investments in fixed assets and the repayment of loans.
- Increase in trade accounts receivable, due to growth in passenger sales.
- Growth in receivables and other current assets, due mainly to the increase in prepaid commissions, due to the increase in passenger sales.
- Decrease in fixed assets, due mainly to periodic depreciation expenses offset by investments in fixed assets made by the Company during the current period, including the \$5.5 million paid by the Company to Boeing as the final payment in the self financing of two model 777-200 planes ordered from Boeing.
- Increase in trade accounts payable, due to the growth in activity, resulting from seasonal changes.
- Increase in payables and other current liabilities, due mainly to the increase in prepaid income, as a result of the increase in sales of not yet utilized air tickets, an increase in airport taxes payable, resulting from the sales growth, and the increase in interest payable, due to the increase in the Libor interest rate.

- The balance of long-term loans (including current maturities) decreased as a result of current repayments of long-term loans.
- Decrease in accrued severance pay, net, due mainly to the deposits by the Company and the State in the severance pay fund, as a result of the exercise of the call options (Series B) of the State and of options (Series 1) of the Company.
- Increase in the Company's shareholders' equity, due mainly to the exercise of options (Series 1) issued by the Company, which led to an increase in share capital and premium on shares, as well as to the deposits by the State of Israel in the severance pay fund, which led to an increase in the capital reserve from transactions with former controlling owners.

**Current ratio by % -
at June 30:**



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



As at June 30, 2007, the Company has a working capital deficit of \$196.6 million, compared with a deficit of \$204.2 million as at December 31, 2006. The Company's current ratio as at June 30, 2007 is 72.7%, compared with 65.0% as at December 31, 2006.

The decrease in the working capital deficit is due to the increase in cash balances and short-term investments, and to the increase in trade accounts receivable, offset by the increase in prepaid income from the sale of not yet utilized air tickets.

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

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

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

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

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

3. Analysis of operating business results of EI AI

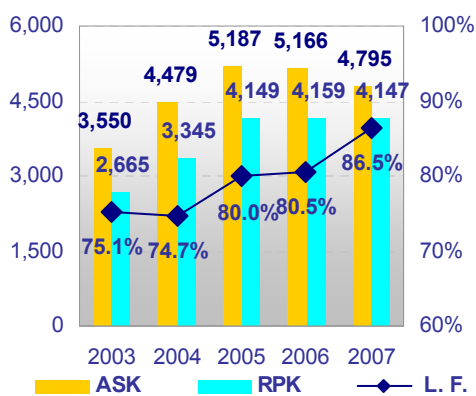
3.1 Market data

Passenger and cargo traffic at BGA	2007		2006		change	
	in thousands	in thousands	in thousands	in thousands	in thousands	%
Apr - Jun						
Incoming tourists *	452	505	(53)	(10%)		
Departing Israelis *	838	802	36	4%		
Cargo import - tons **	33	33	(0)	(1%)		
Cargo export - tons **	47	46	1	2%		
Jan - Jun						
Incoming tourists *	820	891	(71)	(8%)		
Departing Israelis *	1,479	1,363	116	9%		
Cargo import - tons **	66	65	1	2%		
Cargo export - tons **	101	97	4	4%		

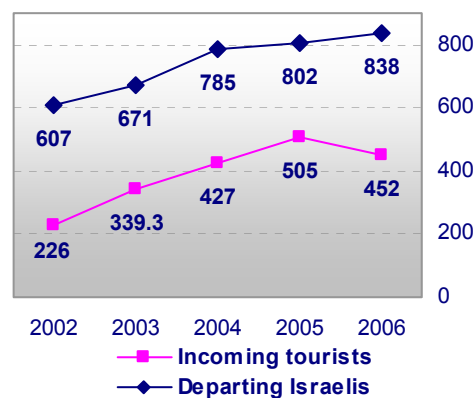
* Source: Central Bureau of Statistics.

** Does not include cargo in transit.

**Operating data,
in second quarter by year:
(in millions)**



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



3.2 Company operating data

	April - June 2007	April - June 2006	Change
Passenger legs (scheduled and chartered) (paying passengers) - in thousands	895	919	(3%)
RPK (scheduled) - in millions	4,147	4,159	(0%)
ASK (scheduled) - in millions	4,795	5,166	(7%)
Load factor (scheduled)	86.5%	80.5%	7%
Company's market share (scheduled and chartered)	36.9%	39.6%	(7%)
Flown cargo, in thousand tons	37	39	(5%)
RTK - in millions	203	207	(2%)
Weighted flying hours (including leased equipment) - in thousands(*)	40.5	44.0	(8%)
<u>Average man-years (EI AI only):</u>			
Permanent	3,529	3,688	(4%)
Temporary	2,287	2,621	(13%)
Total	5,816	6,309	(8%)

	Jan - June 2007	Jan - June 2006	Change
Passenger legs (scheduled and chartered) (paying passengers) - in thousands	1,677	1,741	(4%)
RPK (scheduled) - in millions	7,872	7,953	(1%)
ASK (scheduled) - in millions	9,317	9,787	(5%)
Load factor (scheduled)	84.5%	81.3%	4%
Company's market share (scheduled and chartered)	39.1%	43.2%	(9%)
Flown cargo, in thousand tons	76	85	(11%)
RTK - in millions	407	440	(8%)
Weighted flying hours (including leased equipment) - in thousands(*)	79.7	85.4	(7%)
<u>Average man-years (EI AI only):</u>			
Permanent	3,547	3,674	(3%)
Temporary	2,259	2,530	(11%)
Total	5,806	6,204	(6%)
Aircraft in operation - end of period - number of units	35	35	0
Average age of owned fleet at end of period - in years	15.3	14.7	0.6

Glossary:

Passenger leg – Flight coupon in one direction.

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

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

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

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

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

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

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

3.3 Statement of operations data

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

	April-June 2007		April-June * 2006		change	
	in thousands of dollars	% of operating revenues	in thousands of dollars	% of operating revenues	in thousands of dollars	%
Operating revenues	452,807	100%	429,200	100%	23,607	6%
Operating expenses	(353,901)	(78.2%)	(362,820)	(84.5%)	8,919	(2%)
Gross profit	98,906	21.8%	66,380	15.5%	32,526	49%
Selling expenses	(51,166)	(11.3%)	(47,896)	(11.2%)	(3,270)	7%
General and administrative expenses	(21,887)	(4.8%)	(23,121)	(5.4%)	1,234	(5%)
Operating income (loss) before financing	25,853	5.7%	(4,637)	(1.1%)	30,490	
Financing expenses ,net	(8,255)	(1.8%)	(8,177)	(1.9%)	(78)	1%
Other income (expenses), net	758	0/2%	(1,591)	(0.4%)	2,349	
Income tax savings (expenses)	(5,770)	(1.3%)	3,982	0.9%	(9,752)	
Income (loss) after taxes	12,586	2.8%	(10,423)	(2.4%)	23,009	
Company's equity in results of affiliates, net	47	0.0	53	0.0%	(6)	(11%)
Net income (loss) for the period	12,633	2.8%	(10,370)	(2.4%)	23,003	

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

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

- The increase in operating revenues is due mainly to the increase in passenger revenues, which was offset in part by the decrease in cargo revenues.
- In the second quarter of 2007, there was a decrease in the Company's operating expenses compared with the same period last year, due mainly to the decrease in salary expenses and in most of the operating expenses, such as: airport fees and services and aircraft maintenance expenses, except for jet fuel expenses. This decrease was due mainly to the operating efficiency measures instituted, as expressed in the improved occupancy rates in passenger aircrafts, from 80.5% in the same period last year to 86.5% in the reported period.

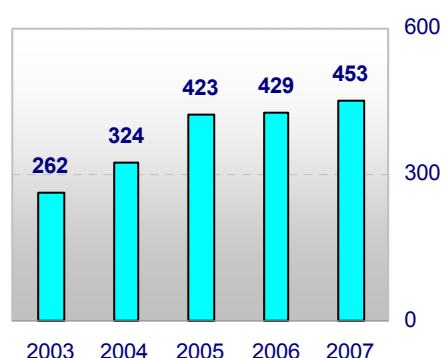
Salary expenses in the reported quarter decreased, as noted, compared with the same quarter last year, due mainly to the reduction in the number of employees in Israel and overseas, the decrease in salary costs and to the increase in the profits of the severance pay funds, even though the appreciation of the shekel and the euro against the dollar during the quarter increased salary expenses.

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

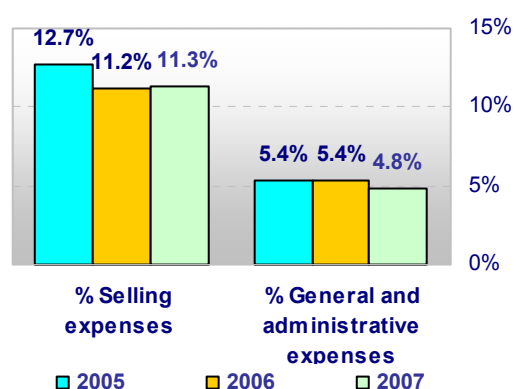
- The Company's expenses for jet fuel rose in the second quarter of 2007 to \$120.1 million, after payments received for hedging totaling \$2.7 million, compared with the same quarter last year, in which they totaled \$116.6 million (after receiving payments for hedging of \$18.4 million). Jet fuel expenses in the reported quarter account for 26.5% of the Company's turnover, compared with 27.2% in the same quarter last year.

- Selling expenses increased as a result of the growth in passenger sales, although their percentage of turnover in the reported period remained similar to their rate in the same quarter last year.
- The administrative and general expenses decreased, mainly due to the reduction in the salary item and to the efficiency and savings measures instituted by the Company. Their percentage of turnover fell from 5.4% in the same quarter last year to 4.8% this quarter.

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



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



- The growth in financing expenses was due to the increase in Libor interest rates and to the expenses for interest hedge transactions, which were offset by the increase in interest income on deposits, as well as by the devaluation of the shekel against the dollar, compared with appreciation that occurred in the same period last year.
- In the current period, the Company recorded other income, net, of \$0.8 million, compared with other expenses, net, of \$1.6 million in the same quarter last year. Most of the income in the current quarter is due to refunds received from Boeing related to the overall accounting between the parties. On the other hand, an expense of \$6.0 million was recorded for an additional early retirement plan.
- In the second quarter of 2007, income tax expenses of \$5.8 million were recorded, compared with tax savings of \$4.0 million in the same quarter last year, due to the net decrease in deferred taxes payable.

Statement of operations data

For the six month period ended June 30, 2007 (consolidated):

	<u>January-June</u> 2007		<u>January-June</u> * 2006		<u>change</u>	
	in thousands of dollars	% of operating revenues	in thousands of dollars	% of operating revenues	in thousands of dollars	%
Operating revenues	841,441	100%	801,749	100%	39,692	5%
Operating expenses	(695,001)	(82.6%)	(675,156)	(84.2%)	(19,845)	3%
Gross profit	<u>146,440</u>	17.4%	<u>126,593</u>	15.8%	<u>19,847</u>	16%
Selling expenses	(93,461)	(11.1%)	(89,041)	(11.1%)	(4,420)	5%
General and administrative expenses	(44,377)	(5.3%)	(45,524)	(5.7%)	1,147	(3%)
Operating income (loss) before financing	8,602	1.0%	(7,972)	(1.0%)	16,574	
Financing expenses, net	(16,649)	(2.0%)	(15,135)	(1.9%)	(1,514)	10%
Other income (expenses), net	6,619	0.8%	(1,277)	(0.2%)	7,896	
Income tax savings	<u>334</u>	0.0%	<u>4,899</u>	0.6%	(4,565)	(93%)
Loss after taxes	(1,094)	(0.1%)	(19,485)	(2.4%)	18,391	(94%)
Company's equity in results of affiliates, net	<u>91</u>	0.0%	<u>95</u>	0.0%	(4)	(4%)
Loss for the period	(1,003)	(0.1%)	(19,390)	(2.4%)	18,387	(95%)

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

The key factors that influenced the business results in the six-month period ended June 30, 2007 compared with the same period last year.

- The increase in operating revenues is due mainly to the increase in passenger revenues and to the increase in other income, such as the sale of duty-free items and maintenance services provided to outside parties, which were offset in part by the decrease in cargo revenues.
- In the first half of 2007, there was an increase in the Company's operating expenses compared with the same period last year, due mainly to the devaluation of the dollar against the shekel and the euro, which increased the Company's shekel expenses in dollar terms for salary and other operating expenses, to the increase in jet fuel expenses and to the increase in aircraft lease fees. However, it should be noted that operating expenses as a percentage of turnover fell from 84.2% in the first half of 2006 to 82.6% in the first half of 2007, mainly as a result of the operating efficiency measures that were expressed in improved passenger occupancy rates – from 81.3% in the first half of 2006 to 84.5% in the reported period.

Salary expenses in the first half of 2007 decreased, compared with the same period last year, despite the devaluation that occurred during the period in the exchange rates of the dollar against the shekel and the euro, which increased salary expenses. This decrease was achieved as a result of the reduction in the number of employees and the decrease in salary costs, and to the increase in the profits of the severance pay funds.

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

- The Company's expenses for jet fuel rose in the first half of 2007 compared with the first half of 2006, from \$214.6 million to \$234.7 million, after hedge payments of \$3.4 million in the first half of 2007 (compared with the receipt of hedge payments of \$34.5 million in the first half of 2006). Jet

fuel expenses in the first half of 2007 account for 27.9% of the Company's turnover, compared with 26.8% in the same period last year.

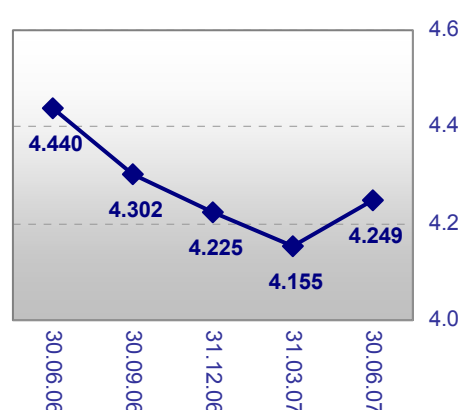
- Aircraft lease expenses increased, mainly as a result of the addition of a 767-300 aircraft that was placed in service in November 2006.
- Selling expenses in the first half of 2007 increased, although their percentage of turnover in the current period remained unchanged in comparison with their percentage of turnover in the same period last year.
- The administrative and general expenses decreased, mainly due to the reduction in salary expenses and their percentage of turnover in the current period decreased compared with their percentage in the same period last year.
- The increase in Libor interest rates led to an increase in financing expenses, which were offset by the decrease in the Company's loan balances, and by the increase in the financing income on the Company's deposits, as a result of the increase in interest rates.
- In the first half of 2007, tax savings of \$0.3 million were recorded, compared with tax savings of \$4.9 million in the first half of 2006, due to the net decrease in deferred taxes payable.
- In the current period, the Company recorded other income, net, of \$6.6 million, compared with other expenses, net of \$1.3 million in the first six months of 2006. Most of the income in the current period is due to refunds received from Boeing related to the overall accounting between the parties, as well as from vacating a property used by the Company in Heathrow Airport in London. On the other hand, an expense of \$8 million was recorded for additional voluntary retirement plans.

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

In the three-month period ended June 30, 2007, the exchange rate of the shekel was devalued against the dollar by 2.3%, compared with appreciation in the exchange rate of the shekel against the dollar of 4.8% in the same quarter last year.

In the first half of 2007, there was devaluation in the exchange rate of the shekel against the dollar of 0.6%, compared with appreciation in the exchange rate of the shekel against the dollar of 3.5% in the same period last year.

Changes in US dollar exchange rate:



The Company has liabilities to its employees for severance pay, retirement plans, sick pay, and vacation pay as at June 30, 2007 of \$127 million.

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

In the quarter ended June 30, 2007, expenses for this element decreased by \$1.3 million, compared with the same period last year, in which expenses totaling \$5.7 million were recorded for this element.

In the first half of 2007, expenses for this element were recorded totaling \$0.8 million, compared with the \$4.2 million in such expenses recorded in the same period last year.

Translation of the Hebrew Language financial statements

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

For the three-month period ended June 30:	<u>Before</u>		<u>After</u>	
	<u>neutralizing effect of changes in exchange rate on Company's provisions</u>			
	2007	2006	2007	2006
	(In thousands US dollars)			
Operating expenses	353,901	362,820	354,330	359,267
Gross profit	98,906	66,380	98,477	69,933
Gross margin	21.8%	15.5%	21.7%	16.3%
Selling, general and administrative expenses	73,053	71,017	73,069	70,323
Operating income (loss) before financing	25,853	(4,637)	25,408	(390)
Rate of operating income (loss) before financing	5.7%	(1.1%)	5.6%	(0.1%)
Other income (expenses), net	758	(1,591)	(53)	(138)
Net income (loss) for the period	12,633	(10,370)	11,377	(4,670)
Net income (loss) rate	2.8%	(2.4%)	2.5%	(1.1%)
For the six-month period ended June 30:	<u>Before</u>		<u>After</u>	
	<u>neutralizing effect of changes in exchange rate on Company's provisions</u>			
	2007	2006	2007	2006
	(In thousands US dollars)			
Operating expenses	695,001	675,156	694,213	672,550
Gross profit	146,440	126,593	147,228	129,199
Gross margin	17.4%	15.8%	17.5%	16.1%
Selling, general and administrative expenses	137,838	134,565	137,621	134,056
Operating income (loss) before financing	8,602	(7,972)	9,607	(4,857)
Rate of operating income (loss) before financing	1.0%	(1.0%)	1.1%	(0.6%)
Other income (expenses), net	(6,619)	(1,277)	6,437	(223)
Loss for the period	(1,003)	(19,390)	(180)	(15,221)
Loss rate	(0.1%)	(2.4%)	(0.0%)	(1.9%)

3.5 Segment reporting

Presented below are geographical segment data on a consolidated basis:

Three-month period ended:					
30.06.2007 (unaudited)	North America	Europe	Central Asia and Far East	Rest of world	Total
	(in millions of dollars)				
Revenues **	166.8	194.7	76.1	9.2	446.8
Operating income ***	18.8	34.9	3.9	2.5	60.1
Operating income as % of segment's revenues	11.3%	17.9%	5.1%	27.2%	13.5%
*30.06.2006 (unaudited)					
Revenues **	155.9	188.1	68.0	8.9	420.9
Operating income ***	5.8	25.8	5.8	2.5	39.9
Operating income as % of segment's revenues	3.7%	13.7%	8.5%	28.6%	9.5%
Six-month period ended:					
30.06.2007 (unaudited)	North America	Europe	Central Asia and Far East	Rest of world	Total
	(in millions of dollars)				
Revenues **	296.3	355.1	154.9	19.0	825.3
Operating income ***	14.9	48.8	9.5	5.0	78.2
Operating income as % of segment's revenues	5.0%	13.7%	6.1%	26.5%	9.5%
*30.06.2006 (unaudited)					
Revenues **	278.8	348.4	143.2	17.7	788.2
Operating income ***	5.7	45.9	24.3	5.0	80.8
Operating income as % of segment's revenues	2.0%	13.2%	16.9%	28.1%	10.3%

For year ended:					
* 31.12.2006 (audited)	North America	Europe	Central Asia and Far East	Rest of world	Total
	(in millions of dollars)				
Revenues **	580.4	702.9	313.5	36.6	1,633.4
Operating income ***	14.9	84.1	39.5	8.0	146.6
Operating income as % of segment's revenues	2.6%	12.0%	12.6%	21.8%	9.0%

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

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

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

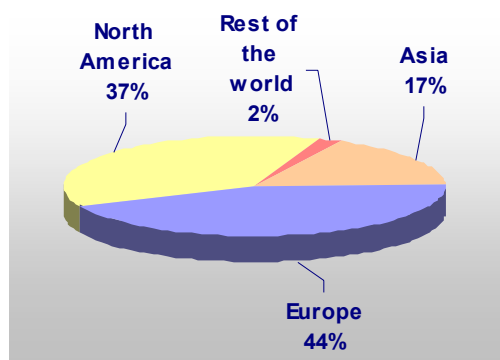
In the three month period ended June 30, 2007 revenues increased in all the geographic segments compared with the same period last year.

The operating income percentages in the second quarter of 2007, compared with the same quarter last year, increased in the North America and Europe segments, whereas they decreased in the Central Asia and Far East and rest of the world segments.

The increase rate of operational profit in the second quarter of 2007 year, in the North America and Europe segments, stems from aircraft passengers. In spite of increase in fuel expenses. The improvement in the North America segment over and above the aforementioned improvements was further improved by direct flight to Los Angeles and Miami.

The reduction in the rate of operational profit, in the Central Asia and Far East segment, stemmed from slowing cargo activity in this area.

**Operating revenues attributed to geographical segments
April – June 2007:**



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

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

4. Seasonal factors

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

5. Liquidity and financing sources

	April – June 2007	April – June *2006	change
	in thousands of dollars	in thousands of dollars	in thousands of dollars
Cash flows from operating activities	72,143	54,919	17,224
Cash flows used for investing activities	(67,615)	(3,946)	(63,669)
Cash flows from (used for) financing activities	17,334	(22,157)	39,491
Net increase in cash and cash equivalents	21,862	28,816	(6,954)

	January – June 2007	January – June 2006*	change
	in thousands of dollars	in thousands of dollars	in thousands of dollars
Cash flows from operating activities	103,998	74,770	29,228
Cash flows used for investing activities	(102,113)	(37,444)	(64,669)
Cash flows from (used for) financing activities	10,904	(30,154)	41,058
Net increase in cash and cash equivalents	12,789	7,172	5,617

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

In the quarter ended June 30, 2007, the Company had cash from operating activities of \$72.1 million (compared with \$54.9 million in the same period last year), after depositing the proceeds of \$22.3 million from the exercise of options in the funded severance pay provision to cover liabilities of the past.

The change in the Company's cash flows from operating activities in the three-month period ended June 30, 2007, compared with the same period last year, derives mainly from the income in the current period, compared with a loss in the same quarter last year.

In the first half of 2007, the Company had cash flows from operating activities of \$104.0 million (compared with \$74.8 million in the same period last year), after depositing the proceeds of \$22.5 million from the exercise of options in the funded severance pay provision to cover liabilities of the past.

The change in the Company's cash flows from operating activities in the first half-year of 2007, compared with the same period last year is due mainly to the decrease in the loss for the period.

In the second quarter of 2007, the Company used \$16.3 million for payments on account of the purchase of planes and of fixed assets, spare parts and tools (compared with \$25.8 million in the same period last year). In the current period, the Company invested \$55.1 million, net, in short-term deposits (compared with net reduction in deposit \$22.0 million, in the same period last year).

In the six-month period ended June 30, 2007, the Company used \$37.5 million for payments on account of the purchase of planes and of fixed assets, spare parts and tools (compared with \$71.1 million in the same period last year). In the current period, the Company invested \$68.4 million, net, in short-term deposits (compared with net reduction in deposit \$33.6 million, in the same period last year).

In total, the Company used \$67.6 million for investing activities in the three-month period ended June 30, 2007, compared with \$3.9 million used in investing activities in the same quarter last year.

In the six-month period ended June 30, 2007, the Company used \$102.1 million for investing activities, compared with \$37.4 million in the same period last year.

In the three-month period ended June 30, 2007, the Company received \$31.6 million in proceeds from the exercise of options for shares, while the Company used \$13.6 million to repay long-term loans, compared with \$23.4 million in the same period last year.

In the six-month period ended June 30, 2007, the Company received \$31.8 million in proceeds from the exercise of options for shares, while the Company used \$20.1 million to repay long-term loans, compared with \$29.5 million in the same period last year.

In total, the Company was provided with \$17.3 million from financing activities in the second quarter of the year, compared with the use of \$22.2 million in the same period last year.

In total, the Company was provided with \$10.9 million from financing activities in the first half of the year, compared with the use of \$30.2 million in the same period last year.

In the three month period ended June 30, 2007, the State deposited \$11.1 million in the severance pay fund of the Company's employees pursuant to the terms of the prospectus (compared with \$0.3 million in the same period last year).

In the first half of 2007, the State deposited \$11.1 million in the severance pay fund of the Company's employees pursuant to the terms of the prospectus (compared with \$0.7 million in the same period last year).

Total cash and cash equivalents and short-term investments as at June 30, 2007 amount to \$232.1 million, compared with \$150.8 million as at December 31, 2006 (June 30, 2006 - \$180.1 million).

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

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

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

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

In the current period, there was no change in the corporation's market risks management policy and the means of control from that described in the Report of the Board of Directors on the State of the Corporation's Affairs for the year ended December 31, 2006 and the notes to the financial statements as at such date. Nonetheless, because of the high future price levels of jet fuel, the market risks management committee of the board of directors resolved to temporarily defer the execution of hedges of jet fuel for the years 2008-2009 to a more favorable time, in accordance

with the policy. Subsequent to the balance sheet date, the Company executed several trades, in accordance with the instructions of the board of directors, so that the actual performance is closer to the policy. For details on the policy that was actually implemented, see Par. 6.2, 6.3 and 6.4 below.

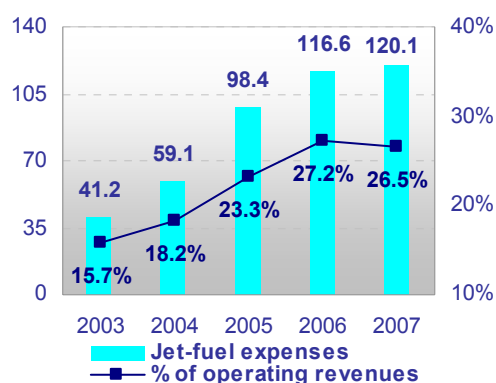
6.2 Hedging jet fuel prices

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

	Type of transaction	Period	Transaction's currency	Fair value in thousand of dollars
HJFP	Financial instruments	Up to One year	US dollar	9,528
HJFP	Financial instruments	Over One year	US dollar	82
Total			US dollar	9,340

For additional information, see Note 21.B.1 of the Periodic Report as at December 31, 2006.

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



6.3 Hedging interest on loans

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

In the current period, no other transactions were executed.

Some of these financial instruments are not recognized for accounting purposes as hedge transactions. The fair value of these instruments as at June 30, 2007 is \$2.5 million, which is stated in the financial statements in the line item "receivables and other assets". Additional agreements are recognized for accounting purposes as hedge transactions.

After executing these hedges, as at June 30, 2007, 60% of the balance of the Company's loans is at fixed interest rates. The percentage of the Company's loans at fixed interest has gradually decreased for a period of up to 4 years.

Translation of the Hebrew Language financial statements

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

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

6.4 Exchange rate hedges

During the reported period, the Company executed several financial transactions intended to protect the Company from decreases in the exchange rate of the dollar against the shekel. These transactions are not recognized for accounting purposes. The fair value of these instruments as at June 30, 2007 is negative fair value of \$0.4 million, which is included in the financial statements in "payables and other liabilities".

6.5 Sensitivity analysis reporting

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

7. Linkage basis report

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

	Denominated in or linked to the dollar	In Israeli currency	Denominated in or linked to the euro	Denominated in or linked to other currencies	Non- monetary items	Total
(in thousands of dollars)						
Assets						
Cash and cash equivalents	136,238	17,328	962	4,419		158,947
Short-term investments	63,500	9,628				73,128
Trade accounts receivable	152,399	94	17,722	19,332		189,547
Receivables and other current assets	16,419	5,198	721	1,508	37,433	61,279
Deferred income taxes					22,041	22,041
Inventory					19,331	19,331
Long-term bank deposits		1,895				1,895
Investment in another company	1,887					1,887
Investees	1,229				1,142	2,371
Fixed assets					1,144,268	1,144,268
Other assets					3,364	3,364
	371,672	34,143	19,405	25,259	1,227,579	1,678,058
Liabilities & Equity						
Short-term borrowings	(100,740)	(517)	(507)	(109)		(101,873)
Trade accounts payable	(107,251)	(24,336)	(18,146)	(11,515)		(161,248)
Payables and other current liabilities	(100,337)	(99,162)	(4,055)	(2,478)	(251,698)	(457,730)
Long-term loans	(548,816)					(548,816)
Accrued severance pay, net	(24,932)	(50,592)	(6,547)	(3,752)		(85,283)
Deferred income taxes					(65,635)	(65,635)
Other long-term liabilities	(563)					(563)
Shareholders' equity					(256,910)	(256,910)
	(882,099)	(174,607)	(29,255)	(17,854)	(574,243)	(1,678,058)
Assets, net of liabilities						
(liabilities net of assets)	(510,248)	(140,465)	(9,851)	7,404	653,336	-

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

	Denominated in or linked to the dollar	In Israeli currency	Denominated in or linked to the euro	Denominated in or linked to other currencies	Non- monetary items	Total
(in thousands of dollars)						
Assets						
Cash and cash equivalents	77,779	19,934	1,138	2,250		101,101
Short-term investments	79,000					79,000
Trade accounts receivable	150,535	257	7,521	8,365		166,678
Receivables and other current assets	13,665	4,554	1,895	1,480	30,399	51,993
Deferred income taxes					21,935	21,935
Inventory					20,116	20,116
Long-term bank deposits		1,815				1,815
Investment in another company	1,945					1,945
Investees	1,229				730	1,959
Fixed assets					1,191,928	1,191,928
Other assets					3,322	3,322
	324,153	26,560	10,554	12,095	1,268,430	1,641,792
Liabilities & Equity						
Short-term borrowings	(63,220)	(272)	(216)	(80)		(63,788)
Trade accounts payable	(95,671)	(25,931)	(16,701)	(8,882)		(147,185)
Payables and other current liabilities	(113,858)	(80,557)	(223)	(320)	(206,213)	(401,171)
Long-term loans	(608,034)					(608,034)
Accrued severance pay, net	(33,664)	(83,436)	(5,552)	(3,464)		(126,116)
Deferred income taxes					(67,423)	(67,423)
Other long-term liabilities	(1,135)					(1,135)
Shareholders' equity					(226,940)	(226,940)
	(915,582)	(190,196)	(22,692)	(12,746)	(500,576)	(1,641,792)
Assets, net of liabilities (liabilities net of assets)						
	(591,429)	(163,636)	(12,138)	(651)	767,854	-

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

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

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

In July 2006, the Israel Accounting Standards Board published Accounting Standard No. 29 – "Adoption of International Financial Reporting Standards (IFRS)" ("the Standard"). The Standard provides that companies that are subject to and report in accordance with the Israeli Securities Law, 1968, will prepare their financial statements in accordance with the International Financial Reporting Standards (IFRS) as from reporting periods commencing January 1, 2008.

The opening balance sheet according to IFRS will be as at January 1, 2007 (Company's transition date to IFRS). The first-time adoption of IFRS Standards will be carried while applying the provisions of IFRS 1 "First-Time Adoption of IFRS Standards", for transition purposes. In financial statements prepared in accordance with IFRS Standards in the year of first-time adoption, the Company is required to present comparative figures for only one year.

The Company is prepared to adopt the IFRS Standards and examined the material effects on the Company expected as a result of the adoption of these Standards. Information on the Company's assessments of the change to reporting according to IFRS Standards and a verbal and qualitative description of the material effects expected on the Company's consolidated financial statements as a result of the change to the International Financial Reporting Standards, including changes that could occur as a result of this transition, are provided by the Company in the Report of the Board of Directors for the year 2006.

For the purpose of these assessments, the Company makes estimates regarding the effect of the transition from generally accepted accounting principles in Israel ("Israeli GAAP") at the date of IFRS reporting. In the nature of things, the assessment process is not yet complete, and its completion is expected with the issue of the financial statements as at December 31, 2007, which will also include a comprehensive quantitative note audited by the independent auditor about the effect of this transition.

Based on the status of the assessments at the reporting date, and subject to the changes that could result from the continuation of the information gathering process and its adjustment to IFRS principles and the changes that could result from developments with respect to IFRS interpretations, presented below is an estimate of the material financial effects of the transition from Israeli GAAP to IFRS on the consolidated financial position of the Company as at January 1, 2007 (the transition date) and its operating results and changes in shareholders' equity from the transition date to June 30, 2007. As noted, since approval of the first financial statements in which IFRS Standards will be applied or information will be disclosed in the financial statements will be in the future. Likewise, disclosure was given about the material financial effects of the transition on the Company's financial position as at June 30, 2007, if these effects are materially different from the effects of the transition on the financial position at the transition date.

It should be emphasized that the information provided below is not reviewed or audited.

For the purpose of determining the estimates related to IFRS, the Company was assisted by the opinion of experts. An actuarial expert appeared before the Company's board of directors and presented the manner in which the calculations pertaining to IAS 19 and their results were prepared. For the purpose of assessing the degree of exposure in legal claims and their impact, the Company received opinions from the attorneys representing them in the claims, including an estimate of their exposure therein, to the extent possible.

Explanations of estimates of the material effects of the transition to application of IFRS on the Company's financial statements:

A. Material effects that will be expressed with the full transition to IFRS reporting:

The results of each of the effects provided below are presented in a table in Par. B. below:

1. According to Israeli GAAP, accrued severance pay is recognized on the basis of the full obligation, assuming that each employee will be dismissed on the balance sheet date at terms that entitled him to full severance pay, without considering the discount rates, the rate of future wage hikes and future terminations. On the IFRS transition date, all of the long-term liabilities for employee severance benefits and other benefit plans are measured in accordance with the provisions of IAS 19 regarding employee benefits. Benefits upon retirement for defined benefit plans are measured, inter alia, based on actuarial estimates and discounted amounts. At the same time, all of the funds defined as "plan assets" are stated at their fair value, in accordance with IAS 19.

Additionally, according to Israeli GAAP, the vacation provision is recognized on the basis of the full obligation, assuming that employees will utilize all the vacation days available to them in the short-term.

On the IFRS transition date, the vacation days expected to be utilized in the short-term are separated from the vacation days expected to be utilized in the long-term, for which the provision is measured on the basis of actuarial estimates and discounted amounts.

The provision for redemption of sick days was calculated in accordance with IFRS rules for all the Company's employees in discounted values.

The effect of the changes regarding this item as at January 1, 2007 is presented in a table in Par. B. in the continuation. The examination of the effect of IAS 19 as at June 30, 2007 and for the six-month period then ended is not yet complete.

2. With respect to contingencies in accordance with Israeli GAAP, the Company recognizes a provision if the use of economic resources to settle the obligation is probable.

According to IFRS, a provision is to be recognized if it is more likely than not that an obligation exists at the balance sheet date. The amount of the provision in IFRS Standards was determined according to the amount that the Company estimates that it will be willing to pay to settle the claim.

3. Differing from Israeli GAAP, according to IFRS, all financial derivatives are recognized as assets or liabilities according to their fair value. The changes in fair value will be charged to the statement of operations (in speculative instruments that do not meet the requirements for recognition as hedge instruments) or shareholders' equity (in instruments earmarked to hedge projected cash flows and meet the requirements for recognition as hedge instruments). To date, it was not the Company's practice to give expression in the balance sheet to the fair value of jet fuel hedge transactions. With the transition to IFRS, these hedges will be presented in the Company's balance sheet at fair value.

The change in the fair value of jet fuel hedges will be charged to a capital reserve, with respect to the "effective" part of the hedge instrument, and to operating expenses in the statement of operations for the part that is not "effective".

According to Israeli GAAP, only the fair value of interest and foreign currency hedges that were not recognized as hedges for accounting purposes were presented in the Company's balance sheet, within the item "receivables" or "payables". According to IFRS Standards, all interest and foreign currency hedges (whether or not recognized as hedges for accounting purposes) will be stated in the consolidated balance sheet at fair value.

The change in fair value of interest and foreign currency hedges will be charged in the financing item in the statement of operations.

4. Options that were issued to investors, the exercise price of which is linked to the CPI and is not denominated in the Company's functional currency, constitute a financial liability because they have an exercise price that is not fixed. Under IFRS, these options should be classified in liabilities and stated at fair value on every balance sheet date, with the changes in fair value charged to the financing item in the statement of operations every period. When these options are exercised, the said liability is added to the premium, so that the underlying shares will be recorded at fair value.

It should be noted that all of the above options were exercised by June 2007.

5. Provision for retirement plan – According to Israeli GAAP, provisions for an early retirement plan are recorded based on management's expectations of their realization. According to IFRS, the retirement plan is recorded only when there is a formal, detailed retirement plan.
6. According to Israeli GAAP, deferred tax assets and provisions were classified as current or non-current assets or current or non-current liabilities, based on the classification of the assets or liabilities for which they were created.

According to IFRS, deferred tax assets and provisions are classified as non-current assets and liabilities (as applicable), even if the expected realization date is short-term.

B. The tables below present estimates of the material effects expected as a result of the transition to International Financial Reporting Standards:

Presented below are consolidated balance sheet data as at January 1, 2007:

01.01.2007										
in thousands US dollars										
	Before IFRS	accrued severance pay IAS 19	Legal claims IAS 37	Fuel hedges IAS 39	Interest hedges IAS 39	Options IAS 32	Retirement plan IAS 19	Total effect influence	Reclassification	IFRS
	Note	A-1	A-2	A-3	A-3	A-4	A-5		A-3 ,A-6	
Assets										
Receivables and other current assets	47,342			5,811				5,811	(2,904)	50,249
Deferred income taxes	30,645			1,368				1,368	(32,013)	
Long-term bank deposits	5,945			19	6,240			6,258	2,904	15,107
Liabilities										
Payables and other current liabilities	(332,691)	28,176	138	(8,812)		(19,930)		(429)		(333,120)
Accrued severance pay, net	(126,171)	(5,026)						(5,026)		(131,197)
Deferred income taxes	(74,603)	(6,019)	(35)		(1,560)			(7,614)	32,013	(50,204)
Other long-term liabilities	(730)			(1,862)				(1,862)		(2,592)
Equity										
Premium on shares	(904)									(904)
Capital reserve	(221,080)			3,476				3,476		(217,604)
Accumulated deficit	139,420	(17,131)	(103)		(4,680)	19,930		(1,984)		137,436

Translation of the Hebrew Language financial statements

Presented below are consolidated balance sheet data as at June 30, 2007:

in thousands US dollars										
	Before IFRS	accrued severance pay * IAS 19	Legal claims IAS 37	Fuel hedges IAS 39	Interest hedges IAS 39	Options IAS 32	Retirement plan IAS 19	Total effect	Reclassification	IFRS
	Note	A-1	A-2	A-3	A-3	A-4	A-5		A-3 ,A-6	
Assets										
Receivables and other current assets	61,279			9,345				9,345	(2,473)	68,151
Deferred income taxes	22,041								(22,041)	
Long-term bank deposits	6,153			82	8,180			8,262	2,473	16,888
Liabilities										
Payables and other current liabilities	(457,730)		(361)	(87)				(448)		(458,178)
Accrued severance pay, net	(85,283)						6,000	6,000		(79,283)
Deferred income taxes	(65,635)		90	(2,687)	(2,045)		(1,560)	(6,202)	22,041	(49,796)
Other long-term liabilities	(563)									(563)
Equity										
Premium on shares	(9,248)					(18,759)		(18,759)		(28,007)
Capital reserve	(233,073)			(5,828)				(5,828)		(238,901)
Accumulated deficit	140,423		271	(825)	(6,135)	18,759	(4,440)	7,630		148,053

* The Company has not yet completed measurement of the effect of IAS 19 as at June 30, 2007, and therefore such data were not included in the table.

Presented below are statement of operations data for the six months ended June 30, 2007 (consolidated):

01.01.2007-30.06.2007 in thousands US dollars										
	Before IFRS	accrued severance pay * IAS 19	Legal claims IAS 37	Fuel hedges IAS 39	Interest hedges IAS 39	Options IAS 32	Retirement plan IAS 19	Total effect		IFRS
	Note	A-1	A-2	A-3	A-3	A-4	A-5			
Operating revenues	841,441									841,441
Operating expenses	(695,001)			1,137				1,137		(693,864)
Gross profit	146,440			1,137				1,137		147,577
Selling expenses	(93,461)									(93,461)
General and administrative expenses	(44,377)		(374)					(374)		(44,751)
Operating income (loss) before financing	8,602		(374)	1,137				762		9,364
Financing expenses, net	(16,649)				1,940	1,172		3,112		(13,537)
Operating income (loss) after financing	(8,047)		(374)	1,137	1,940	1,172		3,874		(4,173)
Other income (expenses), net	6,619						6,000	6,000		12,619
Pre tax income (loss)	(1,428)		(374)	1,137	1,940	1,172	6,000	9,874		8,446
Tax saving (expenses)	334		94	(311)	(485)	0	(1,560)	(2,262)		(1,928)
Income (loss) after taxes	(1,094)		(280)	825	1,455	1,172	4,440	7,612		6,518
Company's equity in results of affiliates, net	91									91
Net Income (loss) for the period	(1,003)		(280)	825	1,455	1,172	4,440	7,612		6,609

* The Company has not yet completed measurement of the effect of IAS 19 for the six month period ended June 30, 2007, and therefore such data were not included in the table.

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

11. Subsequent events

Regarding subsequent events (financing agreements and the purchase of aircrafts and deposits in severance pay fund), see Note 8 to the interim financial statements.

Prof. Israel (Izzy) Borovich

Chairman of the Board

Haim Romano

Chief Executive Officer

August 15, 2007

El Al Israel Airlines Ltd.

Condensed Consolidated Interim Financial Statements

As of June 30, 2007

(Unaudited)

El Al Israel Airlines Ltd.

Table of Contents

	<u>Page</u>
Auditors' Review Report	C-1
<u>Condensed Unaudited Interim Consolidated Financial Statements in US dollars</u>	
Consolidated Balance Sheets	C-2 – C-3
Consolidated Statements of Operations	C-4
Statements of Changes in Shareholders' Equity	C-5 – C-6
Consolidated Statements of Cash Flows	C-7 – C-8
Notes to the Interim Consolidated Financial Statements	C-9 – C-23



בריתמן אלמגור
מרכז עזריאלי 1
תל אביב 67021
ת.ד. 16593, תל אביב 61164

טל: +972 (3) 608 5555
פקס: +972 (3) 609 4022
info@deloitte.co.il
www.deloitte.com

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

Gentlemen:

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

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

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

We were provided with the reports of other auditors regarding the review of the condensed interim financial statements of subsidiaries, the assets of which constitute approximately 1.1% of the total assets included in the condensed interim consolidated balance sheet, and their revenues from operations constitute 0.4% of total revenues included in the condensed consolidated statements of operations for the periods of six months and three months ended June 30, 2007.

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

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

We draw your attention to the following matters:

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

Respectfully,

Brightman Almagor
Certified Public Accountants

Tel-Aviv, August 15, 2007

El Al Israel Airlines Ltd.

Condensed Consolidated Interim Balance Sheets

	<u>As at June 30</u>		<u>As at</u> <u>December 31</u>
	<u>2 0 0 7</u>	<u>2 0 0 6</u>	<u>2 0 0 6</u>
	<u>Unaudited</u>		<u>Audited</u>
	<u>(in thousand US dollars)</u>		
<u>Current assets</u>			
Cash and cash equivalents	158,947	101,101	146,158
Short-term investments	73,128	79,000	4,682
Trade accounts receivable	189,547	166,678	132,544
Receivables and other current assets	61,279	51,993	47,342
Deferred taxes	22,041	21,935	30,645
Inventory	19,331	20,116	17,190
	<u>524,273</u>	<u>440,823</u>	<u>378,561</u>
<u>Investments</u>			
Long-term bank deposits	1,895	1,815	1,836
Investment in another company	1,887	1,945	1,829
Investees	2,371	1,959	2,280
	<u>6,153</u>	<u>5,719</u>	<u>5,945</u>
<u>Fixed assets</u>			
	<u>1,144,268</u>	<u>(*) 1,191,928</u>	<u>(*) 1,176,528</u>
<u>Other assets</u>			
	<u>3,364</u>	<u>3,322</u>	<u>3,455</u>
	<u>1,678,058</u>	<u>1,641,792</u>	<u>1,564,489</u>

(*) Restated – see Note 1.5.

El Al Israel Airlines Ltd.

Condensed Consolidated Interim Balance Sheets

	As at June 30		As at
	2 0 0 7	2 0 0 6	December 31
	Unaudited		Audited
	(in thousand US dollars)		
<u>Current liabilities</u>			
Short-term borrowings and current maturities	101,873	63,788	105,100
Trade accounts payable	161,248	147,185	144,990
Payables and other current liabilities	457,730	401,171	332,691
	<u>720,851</u>	<u>612,144</u>	<u>582,781</u>
<u>Long-term liabilities</u>			
Long-term loans from financial institutions	548,816	608,034	566,104
Accrued severance pay, net	85,283	126,116	126,171
Deferred income taxes	65,635	(*) 67,423	(*) 74,603
Other long-term liabilities	563	1,135	730
	<u>700,297</u>	<u>802,708</u>	<u>767,608</u>
Total liabilities	<u>1,421,148</u>	<u>1,414,852</u>	<u>1,350,389</u>
<u>Shareholders' equity</u>			
Share capital	155,012	131,536	131,536
Premium on shares	9,248	904	904
Capital reserve from transactions with a former controlling party	229,560	(*) 218,425	(*) 218,498
Capital reserve from an employee options program	3,513	973	2,582
Accumulated deficit	(140,423)	(*) (124,898)	(*) (139,420)
	<u>256,910</u>	<u>226,940</u>	<u>214,100</u>
	<u>1,678,058</u>	<u>1,641,792</u>	<u>1,564,489</u>

(*) Restated – see Note 1.5.

Prof. Israel (Izzy) Borovich
Chairman of the Board

Haim Romano
Chief Executive
Officer

Nissim Malki
Chief Financial Officer

Approval date of the financial statements – Ben-Gurion Airport, August 15, 2007.

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

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

	Six-month period ended June 30		Three-month period ended June 30		Year ended December 31
	2007	2006	2007	2006	2006
	Unaudited		Unaudited		Audited
(in thousand US dollars)					
Operating revenues	841,441	801,749	452,807	429,200	1,665,446
Operating expenses	695,001	(*) 675,156	353,901	(*) 362,820	(*) 1,394,159
Gross profit	146,440	126,593	98,906	66,380	271,287
Selling expenses	93,461	89,041	51,166	47,896	187,805
General and administrative expenses	44,377	45,524	21,887	23,121	91,952
	137,838	134,565	73,053	71,017	279,757
Operating income (loss) before net financing expenses	8,602	(7,972)	25,853	(4,637)	(8,470)
Net financing expenses	16,649	15,135	8,255	8,177	29,492
Operating income (loss) after net financing expenses	(8,047)	(23,107)	17,598	(12,814)	(37,962)
Other income (expenses), net	6,619	(1,277)	758	(1,591)	(*) (2,764)
Pre-tax income (loss)	(1,428)	(24,384)	18,356	(14,405)	(40,726)
Income tax savings (expenses)	334	(*) 4,899	(5,770)	(*) 3,982	(*) 6,397
Income (loss) after income taxes	(1,094)	(19,485)	12,586	(10,423)	(34,329)
Company's equity in earnings of affiliates, net	91	95	47	53	417
Net income (loss) for the period	(1,003)	(*) (19,390)	12,633	(*) (10,370)	(*) (33,912)
Basic earnings (loss) per share (NIS 1 par value) – in dollars	(0.002)	(*) (0.05)	0.03	(*) (0.03)	(*) (0.08)
Number of shares used in the computation of basic EPS (in thousands)	418,161	400,570	434,246	400,773	400,680
Fully diluted earnings (loss) per share (NIS 1 par value) – in dollars	(0.002)	(0.05)	0.03	(0.03)	(*) (0.08)
Number of shares used in the computation of fully diluted EPS (in thousands)	418,161	400,570	495,721	400,773	400,680

(*) Restated – see Note 1.5.

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

El Al Israel Airlines Ltd.

Condensed Interim Statements of Changes in Shareholders' Equity

	Share capital	Premium on shares	Capital reserve		Accumulated deficit	Total
			(**)	(***)		
<u>(in thousand US dollars)</u>						
Six-month period ended June 30, 2007 (unaudited):						
Balance – January 1, 2007	131,536	904	(*) 218,498	2,582	(*)(139,420)	(*)(214,100)
Receipts on account of Government of Israel debt	-	-	11,062			11,062
Exercise of options into shares	23,476	8,344	-	-	-	31,820
Benefit value of employee options program	-	-	-	931	-	931
Loss for the period	-	-	-	-	(1,003)	(1,003)
Balance – June 30, 2007	<u>155,012</u>	<u>9,248</u>	<u>229,560</u>	<u>3,513</u>	<u>(140,423)</u>	<u>256,910</u>
Three-month period ended June 30, 2007 (unaudited):						
Balance – April 1, 2007	131,681	955	218,498	3,104	(153,056)	201,182
Receipts on account of Government of Israel debt	-	-	11,062	-	-	11,062
Exercise of options into shares	23,331	8,293	-	-	-	31,624
Benefit value of employee options program	-	-	-	409	-	409
Net income for the period	-	-	-	-	12,633	12,633
Balance – June 30, 2007	<u>155,012</u>	<u>9,248</u>	<u>229,560</u>	<u>3,513</u>	<u>(140,423)</u>	<u>256,910</u>

(*) Restated – see Note 1.5.

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

(**) From the employee options plan.

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

El Al Israel Airlines Ltd.**Condensed Interim Statements of Changes in Shareholders' Equity**

	Share capital	Premium on shares	Capital reserve		Accumulated deficit	Total
			(**)	(***)		
<u>(in thousand US dollars)</u>						
Six-month period ended June 30, 2006 (unaudited):						
Balance – January 1, 2006	131,318	826	(*) 217,723	-	(*)(105,508)	244,359
Receipts on account of Government of Israel debt	-	-	702	-	-	702
Exercise of options into shares	218	78	-	-	-	296
Benefit value of employee options program	-	-	-	973	-	973
Loss for the period	-	-	-	-	(*)(19,390)	(*)(19,390)
Balance – June 30, 2006	<u>131,536</u>	<u>904</u>	<u>(*)218,425</u>	<u>973</u>	<u>(124,898)</u>	<u>(*)226,940</u>
Three-month period ended June 30, 2006 (unaudited):						
Balance – April 1, 2006	131,525	900	(*) 218,090	-	(*)(114,528)	235,987
Receipts on account of Government of Israel debt	-	-	335	-	-	335
Exercise of options into shares	11	4	-	-	-	15
Benefit value of employee options program	-	-	-	973	-	973
Loss for the period	-	-	-	-	(*)(10,370)	(*)(10,370)
Balance – June 30, 2006	<u>131,356</u>	<u>904</u>	<u>(*)218,425</u>	<u>973</u>	<u>(*)(124,898)</u>	<u>(*)226,940</u>
Year ended December 31, 2006 (audited):						
Balance – January 1, 2006	131,318	826	(*) 217,723	-	(*)(105,508)	244,359
Receipts on account of Government of Israel debt	-	-	775	-	-	775
Exercise of options into shares	218	78	-	-	-	296
Benefit value of employee options program	-	-	-	2,582	-	2,582
Loss for the year	-	-	-	-	(*)(33,912)	(*)(33,912)
Balance – December 31, 2006	<u>131,536</u>	<u>904</u>	<u>218,498</u>	<u>2,582</u>	<u>(*)(139,420)</u>	<u>(*)214,100</u>

(*) Restated – see Note 1.5.

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

(**) From the employee options plan.

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

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

	Six-month period ended June 30		Three-month period ended June 30		Year ended December 31
	2007	2006	2007	2006	2006
	Unaudited		Unaudited		Audited
	(in thousand US dollars)				
Cash flows – operating activities					
Net income (loss) for the period	(1,003)	(*) (19,390)	12,633	(*) (10,370)	(*) (33,912)
Adjustments required to present net cash flows provided by operating activities (Appendix A)	127,513	(*) 94,445	81,833	(*) 65,315	(*) 132,344
Net cash provided by operating activities, before deposit of proceeds from exercise of options in funded severance pay, to cover liabilities of the past	126,510	(*) 75,055	94,466	(*) 54,945	(*) 98,432
Deposit of proceeds from exercise of options in funded severance pay, to cover liabilities of the past	(22,512)	(285)	(22,323)	(26)	(296)
Net cash provided by operating activities	103,998	(*) 74,770	72,143	(*) 54,919	(*) 98,136
Cash flows – investing activities					
Investment in other assets	(88)	(901)	(88)	(901)	(1,188)
Additions to fixed assets (including general engine overhauls and payments on account of aircrafts)	(37,484)	(*) (71,074)	(16,281)	(*) (25,768)	(*) (128,894)
Refund of investment in fixed assets	3,843	-	3,843	-	-
Proceeds from disposition of fixed assets	197	388	81	179	6,965
Increase (decrease) in short-term deposits, net	(68,446)	33,594	(55,128)	22,000	107,912
Investments in long-term deposits	(206)	(101)	(72)	(33)	(226)
Realization of long-term deposits	129	368	62	297	560
Investment in supplier deposits	(58)	(46)	(32)	(46)	(82)
Redemption of supplier deposits	-	1	-	1	73
Decrease in investments and loans to investees, net	-	327	-	325	326
Net cash used for investing activities	(102,113)	(*) (37,444)	(67,615)	(*) (3,946)	(*) (14,554)
Cash flows – financing activities					
Proceeds from exercise of options into shares	31,820	296	31,624	15	296
Receipt of long-term loans from financial institutions	-	-	-	-	40,000
Repayment of long-term loans from financial institutions	(18,846)	(28,475)	(12,972)	(22,850)	(67,745)
Receipt of other long-term loans	-	-	-	-	1,014
Repayment of other long-term loan	(1,234)	(1,035)	(620)	(520)	(2,248)
Payment on account of costs of obtaining loans	-	-	-	-	(1,080)
Increase (decrease) in short-term borrowings, net	(836)	(940)	(698)	1,198	(1,590)
Net cash provided by (used for) financing activities	10,904	(30,154)	17,334	(22,157)	(31,353)
Increase in cash and cash equivalents	12,789	7,172	21,862	28,816	52,229
Cash and cash equivalents at beginning of period	146,158	93,929	137,085	72,285	93,929
Cash and cash equivalents at end of period	158,947	101,101	158,947	101,101	146,158

(*) Restated – see Note 1.5.

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

El Al Israel Airlines Ltd.

Condensed Consolidated Interim Statements of Cash Flows

Six-month period ended June 30		Three-month period ended June 30		Year ended December 31
2007	2006	2007	2006	2006
Unaudited		Unaudited		Audited

(in thousand US dollars)

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

Income and expenses not involving cash flows:

Depreciation and amortization (including disposal of accessories, components no longer in use and consumption of supplies)	66,164	(*) 67,225	32,174	(*) 33,521	(*) 134,150
Adjustment in the value of long-term deposits	18	(63)	41	(90)	(151)
Equity in earnings of affiliates, net	(91)	(95)	(47)	(53)	(417)
Increase (decrease) in accrued severance pay, net	(2,992)	3,627	(1,023)	5,067	5,633
Increase in capital reserve from employee options plan	931	973	409	973	2,582
Capital gains (losses) from disposition of fixed assets, net	1,563	(118)	(58)	(51)	(*) (1,642)
Adjustment in value of supplier deposits	-	(22)	-	(23)	58
Deferred taxes	(364)	(*) (4,980)	5,725	(*) (4,025)	(*) (6,510)

Changes in assets and liabilities:

Increase in trade accounts receivable	(57,003)	(41,015)	(22,503)	(5,411)	(5,844)
Decrease (increase) in receivables and other current assets	(15,542)	(5,125)	(6,376)	1,109	93
Decrease (increase) in inventory	(2,141)	2,329	(404)	(2,637)	5,255
Increase (decrease) in trade accounts payable	16,258	(7,861)	12,305	11,030	(10,056)
Increase in payables and other current liabilities	120,717	79,573	61,589	25,900	9,228
Increase (decrease) in other long-term liabilities	(5)	(3)	1	5	(35)
	<u>127,513</u>	<u>(*) 94,445</u>	<u>81,833</u>	<u>(*) 65,315</u>	<u>(*) 132,344</u>

Appendix B – Non-cash transactions:

Government of Israel deposits to the employees' severance-pay fund	<u>11,062</u>	<u>702</u>	<u>11,062</u>	<u>335</u>	<u>775</u>
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(*) Restated – see Note 1.5.

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

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

Note 1 – Reporting principles and accounting policies

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

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

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

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

	Consumer Price Index in points	Dollar-NIS rate in NIS	Dollar-Euro rate in Euro
	<u>%</u>	<u>%</u>	<u>%</u>
As at June 30, 2007	186.67	4.249	0.744
As at June 30, 2006	187.92	4.440	0.787
As at December 31, 2006	184.87	4.225	0.759
Percentage of change –	<u>%</u>	<u>%</u>	<u>%</u>
For the six-month period ended			
June 30, 2007	1.0	0.6	(2.0)
June 30, 2006	1.6	(3.5)	(6.9)
For the three-month period ended			
June 30, 2007	1.2	2.3	(0.9)
June 30, 2006	1.0	(4.8)	(4.5)
For the year ended December 31, 2006	(0.1)	(8.2)	(10.2)

El Al Israel Airlines Ltd.

Notes to the Condensed Consolidated Interim Financial Statements

Note 1 – Reporting principles and accounting policies (continued)

1.3 First-time application of new Accounting Standards –

1.3.1 Accounting Standard No. 27 – Fixed Assets

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

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

After the initial recognition, the Standard allows an entity to apply in its accounting policy, the measurement of fixed assets by the cost method or the revaluation method, provided that it is applied consistently for every fixed asset item in the same category.

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

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

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

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

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

El Al Israel Airlines Ltd.

Notes to the Condensed Consolidated Interim Financial Statements

Note 1 – Reporting principles and accounting policies (continued)

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

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

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

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

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

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

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

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

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

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

1.3.2 Accounting Standard No. 26 – Inventory

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

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

El Al Israel Airlines Ltd.

Notes to the Condensed Consolidated Interim Financial Statements

Note 1 – Reporting principles and accounting policies (continued)

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

1.3.2 Accounting Standard No. 26 – Inventory (continued)

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

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

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

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

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

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

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

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

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

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

El Al Israel Airlines Ltd.

Notes to the Condensed Consolidated Interim Financial Statements

Note 1 – Reporting principles and accounting policies (continued)

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

1.3.4 Accounting Standard No. 30 – Intangible Assets

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

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

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

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

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

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

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

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

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

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

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

El Al Israel Airlines Ltd.

Notes to the Condensed Consolidated Interim Financial Statements

Note 1 – Reporting principles and accounting policies (continued)

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

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

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

1.5 Restatement -

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

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

1. The cost of general overhaul of engines was separated from the original cost of the aircraft and depreciated based on the period of economic benefit from the overhaul (an average of 8 years).
2. The cost of subsequent overhaul is capitalized in fixed assets and is depreciated, as aforesaid, compared with the accounting policy practiced until the Standard took effect, whereby the overhaul was charged to operating expenses.
3. A capital gain recorded in 2006 on the sale of a cargo plane was retroactively adjusted, as a result of the change in the net book value of that plane on the date of sale.
4. An increase in fixed assets as at December 31, 2006 and June 30, 2006 required an accrual of deferred taxes payable of \$7,147 thousand and \$7,063 thousand, respectively.

Likewise, within the scope of processing fixed assets data, it was found that the depreciation differences that were taken into account in the past for calculating the deferred tax liability must be changed. This change increases the deferred tax liability as at December 31, 2006 and June 30, 2006 by additional amounts of \$37,188 thousand and \$38,853 thousand, respectively.

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

The effect on the financial statements of the restatement for the above matters is as follows:

A. Balance sheets

	As at June 30, 2006			As at December 31, 2006		
	Before	Effect of	As reported	Before	Effect of	As reported
	restatement	restatement	in these	restatement	restatement	in these
	(in thousand US dollars)			(in thousand US dollars)		
	(Unaudited)					
Fixed assets	1,164,551	27,377	1,191,928	1,148,389	28,139	1,176,528
Deferred taxes payable	(21,507)	(45,916)	(67,423)	(30,268)	(44,335)	(74,603)
Capital reserve from transactions with former controlling owner	(299,821)	81,396	(218,425)	(299,894)	81,396	(218,498)
Accumulated deficit	187,755	(62,857)	124,898	204,620	(65,200)	139,420
Total shareholders' equity	(245,479)	18,539	(226,940)	(230,296)	16,196	(214,100)

B. Statements of operations:

	For the period of six months ended June 30, 2006			For the period of three months ended June 30, 2006			For the year ended December 31, 2006		
	Before	Effect	After	Before	Effect	After	Before	Effect	After
	restate-	of restate-	restate-	restate-	of restate-	restate-	restate-	of restate-	restate-
	(in thousand US dollars)			(in thousand US dollars)			(in thousand US dollars)		
	Unaudited			Unaudited					
Operating expenses	678,317	(3,161)	675,156	363,484	(664)	362,820	1,402,652	(8,493)	1,394,159
Other expenses (income), net	1,277	-	1,277	1,591	-	1,591	(1,806)	4,570	2,764
Tax savings (expenses)	(51)	4,950	4,899	(40)	4,022	3,982	(134)	6,531	6,397
Loss for the period	27,501	(8,111)	19,390	15,056	(4,686)	10,370	44,366	(10,454)	33,912
Basic and fully-diluted loss per share	0.07	(0.02)	0.05	0.04	(0.01)	0.03	0.11	(0.03)	0.08

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

C. Statement of cash flows:

	For the period of six months ended June 30, 2006			For the period of three months ended June 30, 2006			For the year ended December 31, 2006		
	Before restate- ment	Effect of restate- ment	After restate- ment	Before restate- ment	Effect of restate- ment	After restate- ment	Before restate- ment	Effect of restate- ment	After restate- ment
	(in thousand US dollars)			(in thousand US dollars)			(in thousand US dollars)		
	<u>Unaudited</u>			<u>Unaudited</u>					
Cash flows provided by operating activities	63,470	11,300	74,770	50,319	4,600	54,919	73,436	24,700	98,136
Cash flows provided by (used for) investing activities	(26,144)	(11,300)	(37,444)	654	(4,600)	(3,946)	10,146	(24,700)	(14,554)

Note 2 – Seasonal factors

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

Note 3 – Fixed assets

In the current period, the Company paid \$5.5 million to Boeing as the last payment on account of the independent financing of two model 777-200 aircrafts ordered from Boeing.

In early March 2007, the Company signed an agreement with financing banks for the purchase of two 777-200 aircrafts. At the same time, the Company submitted a request to replace the preliminary liability with a final liability to the EXIM Bank, in order to receive an EXIM guarantee for financing the purchase.

Regarding a subsequent event – see Note 8.1.

Note 4 – Share capital and premium

The options (Series 1 and Series B) were exercisable until June 5, 2007.

In the period of six months ended June 30, 2007, the public exercised 94,930,801 options (Series 1) for the identical number of ordinary shares, NIS 1 par value, that were issued by the Company, in consideration for \$31,820 thousand.

In the period of three months ended June 30, 2007, the public exercised 94,317,226 options (Series 1) for the identical number of ordinary shares, NIS 1 par value, that were issued by the Company, in consideration for \$31,624 thousand.

El Al Israel Airlines Ltd.

Notes to the Condensed Consolidated Interim Financial Statements

Note 4 – Share capital and premium (continued)

The proceeds received by the Company from the exercise of the options (Series 1) were deposited in the severance pay fund of eligible employees, except for the sum of \$8.5 million not yet deposited, and which were included in short-term deposits as at June 30, 2007. Of this sum, the Company made a deposit subsequent to the balance sheet date of \$1.9 million in the severance pay fund of eligible employees, constituting a supplement for the "deficit" specified in the severance pay fund of eligible employees, after the deposit made by the State in July 2007, as discussed in Note 8.2 below.

The Company is evaluating the existence of limitations relating to the ability to use the balance of the proceeds, pursuant to the agreement between it and the State and representatives of the employees which was signed on the eve of the Company's privatization.

Likewise, in the period of three months ended June 30, 2007, the State made a deposit thousand in the severance pay fund for eligible employees of \$11,062, which originated in the exercise of the options (Series B) by the public, pursuant to the agreement between it and the State and representatives of the employees which was signed on the eve of the Company's privatization.

Regarding a subsequent event – see Note 8.2.

Note 5 – Legal proceedings

5.1 Class actions

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

5.1.1. In October 1998, a claim was lodged in Nazareth District Court against the Company, as well as a motion for recognition as a class action, in the amount of NIS 230.4 million (\$54.2 million as at the balance sheet date).

The claim related to an allegation of overcharging for airline tickets by travel agents, which the plaintiff alleges were created by using improper exchange rates. In 2002, the Court recognized the motion to recognize the claim as a class action in the context of the Consumer Protection Law. The Company filed a motion for leave of appeal with the Supreme Court. The Company is not expected to be found liable in this claim. A provision for this claim is not included in the financial statements.

5.1.2. In September 1999, a claim was lodged in Tel-Aviv District Court against the Company and against the Airport Authority and Ophir Tours (a travel agency), as well as a motion for recognition as a class action, in the amount of NIS 21.7 million (\$5.1 million as at the balance sheet date). The plaintiff alleges that the travel agency collected the passenger's fee from it using an exchange rate exceeding the legal rate for this purpose, which is the representative exchange rate, and that the Company is responsible for the actions of the agents in this matter. In 2002, the Court approved the motion for class action recognition in the matter of breach of legislated duty based on Regulation 29 of the Civil Procedure Regulations. The Company filed a motion for leave of appeal with the Supreme Court.

El Al Israel Airlines Ltd.

Notes to the Condensed Consolidated Interim Financial Statements

Note 5 – Legal proceedings (continued)

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

Consequently, the parties were asked to submit their positions to the Court with respect to continuing the proceedings. The plaintiff announced that it wishes to continue the hearings based on a cause of action from the Consumer Protection Law, which was not approved in District Court. The Court has not yet ruled on this issue. At this stage, in the estimation of the Company, and based on the opinion of its legal counsel, it is not possible to assess the outcome of the appeal, and the outcome of the claim itself. No provision was included for this claim in the financial statements.

5.2 Anti-trust lawsuits abroad

- 5.2.1 In February 2006, the Anti-Trust Department of the U.S. Justice Department ("Anti-Trust Department") instituted an open investigation, together with other such authorities in other countries, for alleged suspicion of price fixing regarding certain increments in air cargo transport prices. Several cargo airlines announced that they had received grand jury subpoenas in connection with this investigation. On September 27, 2006, the Company received a grand jury subpoena from the Anti-Trust Department, demanding information and documents related to the pricing practice and to certain price increments related to flying cargo, from early 1999 until the subpoena date. The Anti-Trust Department informed the Company that the Company would be investigated as a suspect in this investigation. The Company is cooperating with the investigation, while performing an internal investigation of cargo pricing practices. At this stage, the Company is unable to assess the outcome of the Anti-Trust Department's investigation or the possible financial impact of the investigation. However, it should be noted that the implications could include administrative and/or civil proceedings, and/or a criminal indictment, including penalties and/or civil liability. It is also stated that the penalties for violation of Anti-Trust laws could be serious, with respect to the legal liability and the civil liability.
- 5.2.2 In December 2006, the Company received a letter from the European Anti-Trust Commission ("the Commission"), which was delivered to the Company's offices in Germany, demanding information in connection with the investigation being conducted by the Commission. The letter stated that the demand for information was within the scope of an investigation that the Commission is conducting with respect to activities that allegedly hurt competition in the air cargo transport services sector, and that the Commission has information on extensive contacts maintained between the airlines and other bodies pertaining to various price increments and other matters, such as the tariffs for cargo transport.

El Al Israel Airlines Ltd.

Notes to the Condensed Consolidated Interim Financial Statements

Note 5 – Legal proceedings (continued)

5.2 Anti-trust lawsuits abroad (continued)

The letter asked the Company to transfer data and documents relating to the Company and its cargo activities since 1995. The Company is cooperating with the investigation and sent its response, as requested by the Commission's letter, while it is also conducting an independent internal examination of the cargo pricing practices. At this juncture, the Company is unable to assess the outcome of the Commission's investigation or to estimate the investigation's possible financial impact on the Company.

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

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

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

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

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

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

5.3 Additional claims

5.3.1 On January 22, 2007, a claim was filed against the Company in Jerusalem District Court, together with a motion for recognition as a class action, in the amount of NIS 483.4 million (\$113.8 million as at the balance sheet date).

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

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

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

El Al Israel Airlines Ltd.

Notes to the Condensed Consolidated Interim Financial Statements

Note 5 – Legal proceedings (continued)

5.3 Additional claims (continued)

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

Note 6 – Other income and expenses

- 6.1 As a result of the discontinuation of operations of a company related to Boeing, with which the Company had an undertaking in the past to operate Internet systems on some of the Company's aircraft, the Company discontinued the providing of such service. In January 2007, an agreement was signed between the Company and Boeing, whereby the Company received damages from Boeing for its investments in the Internet system, and the additional damages it sustained due to discontinuation of the system's operation. As a result of these damages, the Company recorded income in the period of three months ended March 31, 2007 of \$4.4 million, which was charged to "other income".
- 6.2 In March 2007, the Company signed an agreement with the British Aviation Authority, whereby a property that had been used in Heathrow Airport in London was vacated, and accordingly, it received early vacancy fees from the above Aviation Authority.
As a result of this agreement, the Company recorded net income (after taxes) of \$3.4 million in the period of three months ended March 31, 2007, which was charged to "other income".
- 6.3 In July 2007, a clarification to an agreement between the Company and Boeing was signed, with respect to an overall accounting between the parties. Within this framework, there was agreement that the sum of \$6.5 million of the cash flows, which were or are expected to be received by the Company from Boeing constitute damages for the loss of revenues sustained by the Company due to the discontinuation of two joint projects, including the project for broadband Internet in planes. This amount was included in the Company's other income in the period of three months ended June 30, 2007.
- 6.4 Other expenses for the period of three months ended June 30, 2007 include a provision for the early retirement plan for an additional 60 employees, totaling \$6 million. Management expects that most of these employees will be included in the framework of early pension payments, and some will receive increased severance payments.

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

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

	<u>North America</u>	<u>Europe</u>	<u>Far East and Central Asia</u>	<u>Rest of the world</u>	<u>Total</u>
	(in thousand US dollars)				
For the period of six months ended 30.6.07 (unaudited)					
Revenues -					
Revenues by segment	<u>296,297</u>	<u>355,105</u>	<u>154,926</u>	<u>18,999</u>	825,327
Revenues not allocated to segments					<u>16,114</u>
Total revenues - consolidated					<u>841,441</u>
Operating income -					
Operating income by segment	<u>14,883</u>	<u>48,819</u>	<u>9,462</u>	<u>5,033</u>	78,197
Expenses of all segments, net					<u>(69,595)</u>
Operating income before financing expenses, net - consolidated					<u>8,602</u>
	<u>North America</u>	<u>Europe</u>	<u>Far East and Central Asia</u>	<u>Rest of the world</u>	<u>Total</u>
	(in thousand US dollars)				
For the period of three months ended 30.6.07 (unaudited)					
Revenues -					
Revenues by segment	<u>166,820</u>	<u>194,715</u>	<u>76,077</u>	<u>9,163</u>	446,775
Revenues not allocated to segments					<u>6,032</u>
Total revenues - consolidated					<u>452,807</u>
Operating income -					
Operating income by segment	<u>18,811</u>	<u>34,901</u>	<u>3,915</u>	<u>2,492</u>	60,119
Expenses of all segments, net					<u>(34,266)</u>
Operating income before financing expenses, net – consolidated					<u>25,853</u>

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

	<u>North America</u>	<u>Europe</u>	<u>Far East and Central Asia</u>	<u>Rest of the world</u>	<u>Total</u>
	<u>(in thousand US dollars)</u>				
For the period of six months ended 30.6.06 (unaudited)					
Revenues -					
Revenues by segment	<u>278,805</u>	<u>348,419</u>	<u>143,201</u>	<u>17,747</u>	788,172
Revenues not allocated to segments					<u>13,577</u>
Total revenues - consolidated					<u>801,749</u>
Operating income -					
Operating income by segment (*)	<u>5,687</u>	<u>45,913</u>	<u>24,257</u>	<u>4,986</u>	80,843
Expenses of all segments, net					<u>(88,815)</u>
Operating loss before financing expenses, net - consolidated					<u>(7,972)</u>
			Far East and Central Asia		
	North America	Europe		Rest of the world	Total
	<u>(in thousand US dollars)</u>				
For the period of three months ended 30.6.06 (unaudited)					
Revenues -					
Revenues by segment	<u>155,935</u>	<u>188,103</u>	<u>67,992</u>	<u>8,907</u>	420,937
Revenues not allocated to segments					<u>8,263</u>
Total revenues - consolidated					<u>429,200</u>
Operating income -					
Operating income by segment (*)	<u>5,807</u>	<u>25,751</u>	<u>5,791</u>	<u>2,545</u>	39,894
Expenses of all segments, net					<u>(44,531)</u>
Operating income before financing expenses, net – consolidated					<u>(4,637)</u>

(*) Restated – see Note 1.5.

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

	<u>North America</u>	<u>Europe</u>	<u>Far East and Central Asia</u>	<u>Rest of the world</u>	<u>Total</u>
	<u>(in thousand US dollars)</u>				
For the year ended					
December 31, 2006 (audited):					
Revenues -					
Revenues by segment	<u>580,399</u>	<u>702,909</u>	<u>313,500</u>	<u>36,590</u>	1,633,398
Revenues not allocated to segments					<u>32,048</u>
Total revenues					<u>1,665,446</u>
Operating income -					
Operating income by segment (*)	<u>14,937</u>	<u>84,119</u>	<u>39,535</u>	<u>7,989</u>	146,580
Expenses of all segments, net					<u>(155,050)</u>
Operating loss before financing expenses					<u>(8,470)</u>

(*) Restated – see Note 1.5.

Note 8 – Subsequent events

8.1 During July 2007, a financing agreement was signed opposite banks for the purchase of two model 777-200 aircrafts. Concurrently, a final commitment was received from EXIM to furnish a guarantee to secure this financing.

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

For the second aircraft, which will be delivered to the Company in August 2007, the Company will receive a loan of \$110 million, of which \$86 million is earmarked for payment of the balance of the aircraft's price to Boeing, as well as the costs related to raising the financing. The balance of \$24 million for the part of the independent financing furnished by the Company for the purchase of the aircraft will be returned to the Company.

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

8.2 In July 2007, the State deposited in the severance fund of eligible employees, the final payment received from the State for exercise of options (Series B) totaling \$14 million. Likewise, in August 2007, the Company deposited an additional \$1.9 million in the fund for eligible employees. After these deposits, the "deficit" in the fund for eligible employees, as defined in the agreement between the Company, the State and representatives of the employees, which was signed on the eve of the privatization, was covered.