EL AL ISRAEL AIRLINES LTD.

FINANCIAL STATEMENTS

AS OF MARCH 31, 2006

(unaudited)

SECTION A - UPDATE OF CHAPTER A TO 2005 ANNUAL REPORT

SECTION B - DIRECTOR'S REPORT

SECTION C - FINANCIAL STATEMENTS

FINANCIAL STATEMENTS

AS OF MARCH 31, 2006

SECTION A

UPDATE OF CHAPTER A TO 2005 ANNUAL REPORT

Update of Chapter A (Description of the Entity's Business)[1] to the Periodic Report for the Year 2005 ("The Periodic Report") of El Al Israel Airlines Ltd. (hereafter: "the Company")

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

To Section 6.3-fluctuations in prices of jet fuel, and to Section 9.5.1-raw materials and suppliers-fuel

During the quarter ended March 31, 2006, the market prices of jet fuel rose on the average by approximately 27% relative to the corresponding period last year. During the quarterly period, fuel expenses represented approximately 26% of total revenues (approximately 24% of total revenues during the first quarter of the year 2005).

See Section 6.2 to the Directors' Report concerning the Company's Affairs for further details.

To Section 6.5-fluctuations in interest rates

During the quarter ended March 31, 2006, there was a rise of approximately 10% in the average rate of 3-month LIBOR interest, relative to the average LIBOR rate during the quarter ended on December 31, 2005, and a rise of approximately 68% relative to the corresponding quarter last year.

See Section 6.3 to the Directors' Report concerning the Company's Affairs for further details.

2. The Operating Sector of Passenger Aircraft

To Sections 7.1.4-developments in markets, 7.1.10-structure of competition in the operating sector, including changes, 7.8-competition, 9.11.7.4-capacity, 9.18.3-discussion of risk factors: changes in competition

Continuing what was detailed in these sections in the Periodic Report mentioned in the above header, in the matter of approvals to increase flight capacity to and from Israel given to a line up of foreign airline companies, and in the matter of the denoted trend towards reduction in the restrictions in giving such approvals, it should be stated that, at the end of the first quarter of the year 2006, towards the start of the summer flight schedule, a number of foreign airline companies significantly increased their flight capacity to and from Israel.

In addition, during this period, the Delta and "Happag Lloyd" companies began their scheduled flight operations to Israel, and, in April 2006, the Air Madrid company began to operate charter flights to Israel.

In view of the above, beginning from April 2006, there is a substantial exacerbation of competition in the sector, and the situation could negatively affect the operating results of the Group.

[1] The update is being made in accordance with Regulation 39A of the Securities Regulations (Immediate and Periodic Reports), 1970, and it includes material changes or developments which took place in the entity's operations with regard to any matter which must be described in the Periodic Report. The update relates to the numbers of the sections of Chapter A (Description of the Entity's Business) in the Group's Periodic Report for the year 2005.

It should be noted that the Israir company, which was appointed as an additional Israeli designated carrier for the New York route, started, beginning from May 2006, to operate the 3 weekly flights, which it had previously run as charter flights, as scheduled flights, and, through the date that this report was issued, has not added flight capacity on the route

To Section 7.11-fleet of aircraft in the operating sector of passenger aircraft

Continuing what was said in Section 7.11.1.B to the Periodic Report, in connection with the leasing of a 767-300 ER aircraft commencing from the month of May 2006 for 5 years, it should be mentioned that in the middle of the month of May 2006, the aircraft was turned over to the Company.

In addition to what was itemized in Section 7.11.1 B to the Periodic Report, it should be noted that, in March 2006, the Company signed an agreement to lease an additional 767-300 ER aircraft, commencing from November 2006 for 5 years. The aircraft is approximately 11 years old and, as used by the Group, will contain approximately 235 seats.

3. The Operating Sector of Cargo Aircraft

To Section 6.1-increase in traffic in the international aviation sector, and to Section 8.1.3 (a)- the volume of world cargo transport

According to reports of IATA, during the months of January-February 2006, there was an increase of approximately 5.3% in the volume of world cargo transport in cargo aircraft, as compared with the year 2005, that is, growth at a lower pace than the anticipated annual pace according to estimates of IATA (6.3%). At the same time, it cannot be estimated whether this fact changes expectations as to the overall, annual pace of growth for the year 2006.

To Section 8.1.3 (b)- the volume of cargo transport in aircraft to and from Israel

The data of the Civil Aviation Authority indicate, that in the first quarter, the volume of cargo traffic at BGA decreased by 2.8%, in comparison with the first quarter last year, this as opposed to the estimate of IATA which forecast annual growth in a volume of approximately 5%.

To Section 8.10- fleet of aircraft, and to Section 9.11.9-Special State Share

In accordance with what was stated in Section 8.10, footnote 39, of the Periodic Report, commencing from the month of April 2006, the operations of one of the 747-200C convertible aircraft was terminated and it was offered for sale.
It should be pointed out that, due to the fact that in the context of a negotiation being held for the sale of this aircraft, the possibility of the sale of an additional cargo aircraft is being discussed, and in view of the provisions of the Special State Share, which are itemized in Section 9.11.9, footnote 68, to the Periodic Report, the Company applied to the Government Corporations Authority during the month of April with a request to receive the approval of the holder of the Special State Share for the sale of the fourth cargo aircraft, and for the reduction of the number of the Company's cargo aircraft to three. The Company transmitted information to the Government Corporations Authority which had been requested for purposes of formulating the position of the holder of the Special State Share. Through a date in proximity to the approval of this report, the position of the State had not yet been received.

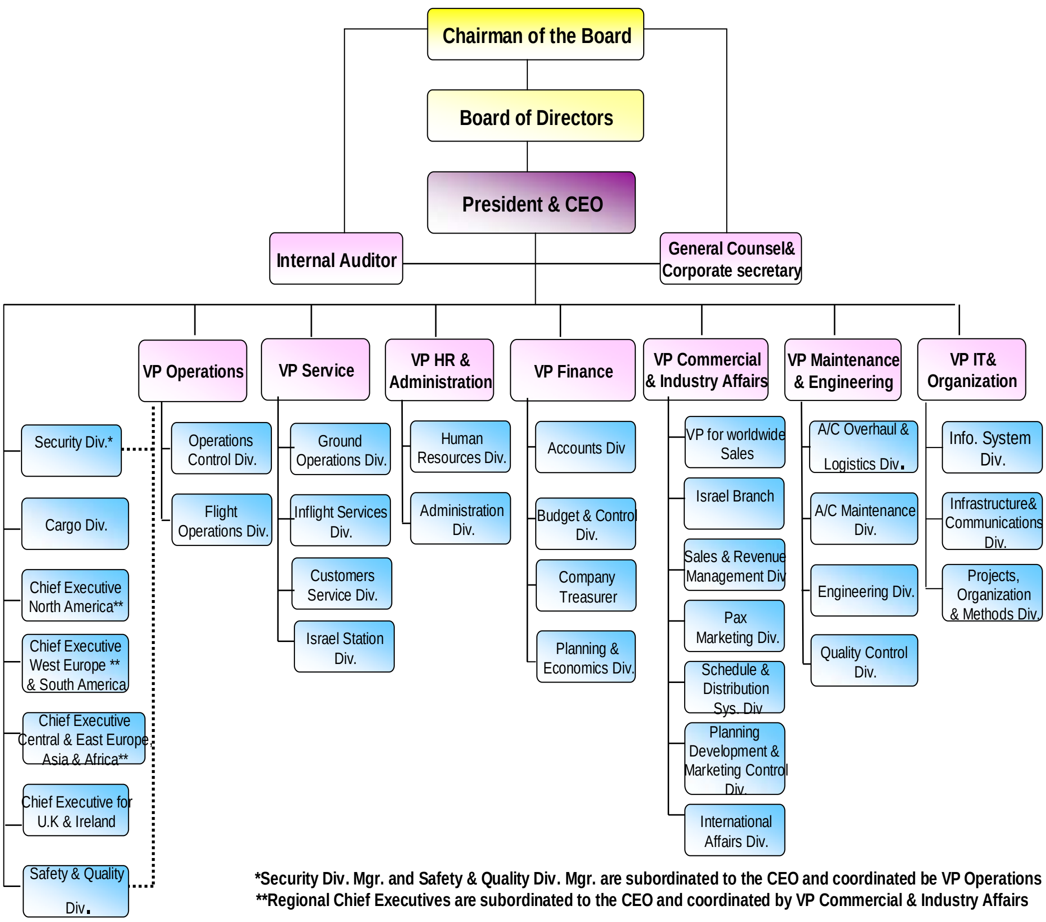
4. **Details Relating to the Two Operating Sectors**

To Section 9.4.1 - the organizational structure, to Section 9.4.2 - the personnel employed and to Section 9.4.16 - officers and senior management employees

1. As the Company reported in an Immediate Report dated April 23, 2006, on that date, Mr. Yoav Levy ceased to serve in the position of the VP-Commercial and industry affairs. The Company is in the process of finding a suitable replacement for the position and in the meantime VP for worldwide Sales together with the Head of Division of the Scheduling and Distribution Systems Division are acting as substitutes.

2. In continuation of what was itemized in Section 9.4.1 of the Periodic Report, in April 2006, an Israel Station Division was created, which is subordinate to the VP-Service. As the result of this organizational change, the number of senior employees mentioned in the table in Section 9.4.2 of the Periodic Report rose to 43. The number of members of extended management and additional senior employees, mentioned in the table in Section 9.4.16 of the Periodic Report, was updated to 33.

   The following is a diagram which describes the up-to-date organizational structure of the Company:



<u>To Section 9.4.5-employee compensation program</u>

In continuation of what was itemized in Section 9.4.5. C. of the Periodic Report, on May 23, 2006, the Board of Directors of the Company decided to add 3,000,000 options to the pool of options to be allotted under the options program which was approved on February 26, 2006 ("**the 2006 Options Program**"). Additionally, the Board of Directors appointed the HR and appointment Committee as the Administrator of the 2006 Options Program and authorized the Committee to allot options to executives of the Company in accordance with the guidelines stipulated by the Board of Directors. Also, the Board of Directors approved the publication of an outline, according to which it will be permitted to issue options in accordance with the 2006 Options Program.

See Section 9 to the Interim Financial Statements for additional details.

<u>To Section 9.6.5 - working capital deficit</u>

See updates in Section 2 to the Directors' Report concerning the Company's Affairs for details regarding the working capital deficit and the current ratio of the Company.

<u>To Section 9.11.2.G. - restrictions and supervision of the entity's business-business restrictions</u>

In continuation of what was itemized in Section 9.11.2.G. (3) of the Periodic Report, on March 30,2006, the Company filed an appeal with the Business Restrictions Tribunal regarding the declaration by the Commissioner of Business Restrictions on October 27, 2005, in which the Commissioner declared that the Company was a monopoly as to the transport of time-sensitive passengers and price-sensitive passengers in the civil aviation markets to the destinations: Johannesburg, Hong Kong, Bangkok and Bombay.

The appeal requests the Tribunal to revoke the declaration with regard to the markets which are the subject of the declaration, in full or in part. Among the principal allegations upon which the appeal is based: the assertion that the market definition of the Commissioner is erroneous and disregards the characteristics of competition for flights from Israel to long range destinations in the Far East; the assertion that the analysis by the Commissioner, that related to the substitutability of demand alone, is a deficient and erroneous analysis which ignores the current substitutability from the viewpoint of supply despite it being immediate and lacking sunken costs; the assertion that the judgment used by the Commissioner in his decision to activate his authority to declare a monopoly was wrong from the outset and that the Commissioner erred in the manner in which he used his judgment and in the probability of the results of his declaration; the assertion that even according to the definitions of the market which were adopted by the Commissioner, the Company does not transport in excess of 50% of the passengers between Israel and India.

The Commissioner's response to the appeal has not yet been presented.

In the context of the appeal, the Company also made a request to provide it with the right to study the documents which served the Commissioner when he declared a monopoly, and which were not submitted to the Company due to the objections of third parties. A final decision on this request has not yet been received.

FINANCIAL STATEMENTS
AS OF MARCH 31, 2006

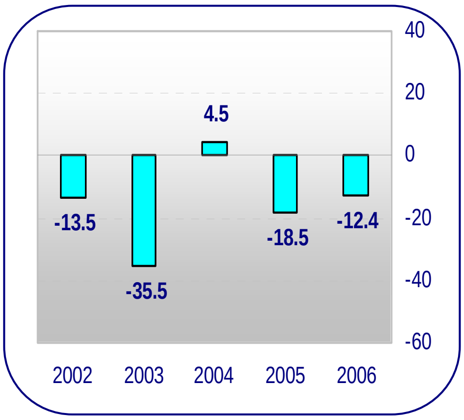
SECTION B

DIRECTOR'S REPORT

EL AL ISRAEL AIRLINES LTD.

REPORT OF THE BOARD OF DIRECTORS CONCERNING THE COMPANY'S AFFAIRS DURING THE THREE - MONTH PERIOD ENDED MARCH 31, 2006

Net income(loss) in the first quarter by year: (in millions US dollars)



We are pleased to submit herewith the directors' report regarding the Company's state affairs on March 31, 2006 and for the three-month period then ended.

The Company recorded a loss of $12.4 million ("m") as compared with a loss of $18.5m in the corresponding period last year.

First-quarter revenues rose by 17% over the same period last year, totaling $373m.

Net cash provided by operating activities in the first quarter amounted to $13.2m, with the balances of cash and short-term investments on March 31, 2006 totaling $173.5m. Shareholders' equity on March 31, 2006 amounted to $259.2m.

1. The Company's business environment

1.1 Overview

The Company serves as Israel's designated carrier on most international routes to and from the country. Most of its activity as well as that of its subsidiaries entails the carrying of passengers and cargo, including baggage and mail, through scheduled flights and, as far as passengers are concerned, also chartered flights between Israel and foreign countries.

The Company is also engaged in the leasing of flight equipment, rendering handling and maintenance services at its home base Ben Gurion Airport ("BGA"), the sale of duty-free products and - through its investees - related activities, the most significant of which constitute the supply of passenger meals and managing several travel agencies in Israel and abroad.

The Company's business environment constitutes, international as well as tourist civil aviation to and from Israel, characterized by seasonal factors and tough competition, which intensifies in periods of excess capacity.

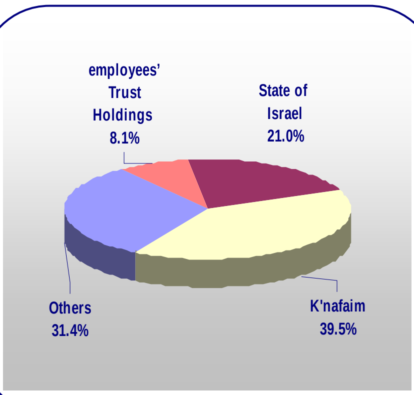
The Company competes with 40 scheduled airlines which operate in the market on the basis of aviation agreements signed between the State of Israel ("the State")and other countries as well as 55 charter airlines which operate based on the charter regulations established by the Ministry of Transport.

The Group operates in the following two business segments:

a) **Air transport - passenger aircraft -** carrying passengers and cargo (including baggage and mail) plus related services, such as the sale of duty-free products and the leasing of passenger aircraft.

b) **Air transport - cargo aircraft -** carrying cargo and providing related services, such as the leasing of cargo aircraft.

Shareholdings in Company at March 31, 2006:



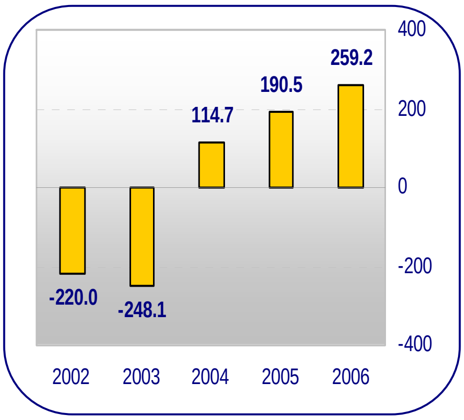
1.2 Privatization

On March 31, 2006 the Company was held by K'nafaim Holdings Arkia Ltd. ("K'nafaim") (39.5%), The state of Israel (21.0%), Holdings in trust of the employees of EL AL Ltd. (the employees' company) (8.1%) and others (31.4%).

As for additional details concerning the Company's privatization - see Note 1.b to the 2005 annual financial statements.

2. Financial position (Consolidated data)

Shareholders' equity at March 31:
(in millions US dollars)

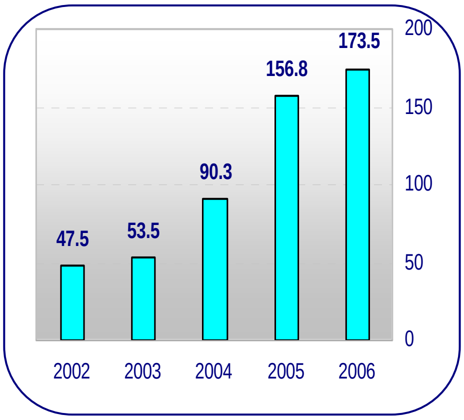


	31.3.2006 in thousands US dollars	31.12.2005 in thousands US dollars	change in thousands US dollars	%
Assets				
Cash and short-term investments	173,523	206,763	(33,240)	(16%)
Trade accounts receivable	159,450	123,846	35,604	29%
Receivables and other current assets	54,918	48,684	6,234	13%
Deferred income taxes	21,758	46,698	(24,940)	(53%)
Inventory	17,480	22,445	(4,965)	(22%)
Investments	5,859	5,846	13	0%
Fixed assets	1,172,911	1,163,765	9,146	1%
Other assets	2,491	4,671	(2,180)	(47%)
	1,608,390	**1,622,718**	**(14,328)**	**(1%)**
Equity & liabilities				
Short-term borrowings	73,845	75,713	(1,868)	(2%)
Trade accounts payable	136,156	155,046	(18,890)	(12%)
Payables and other current liabilities	379,234	324,546	54,688	17%
Long-term loans from financial institutions	619,493	627,363	(7,870)	(1%)
Accrued severance pay, net	117,446	120,526	(3,080)	(3%)
Deferred income taxes	21,333	46,300	(24,967)	(54%)
Other long-term liabilities	1,671	2,215	(544)	(25%)
Shareholders' equity	259,212	271,009	(11,797)	(4%)
	1,608,390	**1,622,718**	**(14,328)**	**(1%)**

The following is an outline pertaining to the major changes in assets, liabilities and shareholders' equity on March 31, 2006 as compared with the balances of December 31, 2005:

- A decrease in cash and short-term investments, stemming mainly from payments on account of aircraft acquisition, investments in fixed assets and loan repayments which has partly been offset by positive cash flows provided by operating activities.
- An increase in trade accounts receivable, mainly due to higher passenger and cargo revenues.
- An increase in receivables and other current assets, stemming mainly from higher prepaid commissions due to an increase in passenger revenues.
- The decrease in deferred income taxes receivable with a concurrent decline in deferred income taxes liability totaling $25m stems from the classification of a tax asset (in respect of carry-forward losses) from short term to long-term receivables.

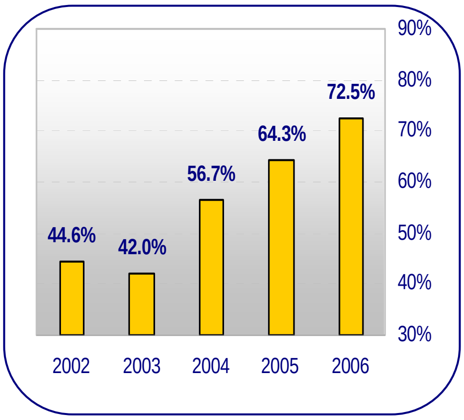
Cash and short-term investments at March 31:
(in millions US dollars)



- A decrease in inventory mainly due to jet-fuel consumption.
- An increase in fixed assets, stemming mainly from a $29m payments on account of aircraft and spare-parts purchases, offset by the periodic depreciation charges.
- A decrease in other assets, mainly explained by the change in the classification of loan-attainment expenses from other assets to a reduction in long-term loans in accordance with Standard No. 22 of the Israeli accounting Standards Board.
- A decrease in trade accounts payable stemming, mainly from a change in the terms of payment to a jet-fuel supplier and one time advanced payments for suppliers abroad.
- A rise in payables and other current liabilities, mainly due to higher deferred income following an increase in sale of tickets not yet realized, as well as an increase accrued expenses due to the higher activity and the increase in interest payable following the global rise in interest rates.
- The balance of long-term loans (including current maturities) has declined mainly due to current repayments.
- Net accrued severance-pay liabilities declined mainly due to payments made on account of early retirement programs, deposits of funds by the Government of Israel and the Company to the severance-pay fund (within the framework of the agreement between the Company, the government and the employees), the shekel's devaluation against the dollar and an increase in the value of severance-pay funds.

- A decrease in shareholders' equity stemming mainly from the loss for the period, net of the noted deposits made by the government to the severance-pay fund, which has raised the "capital reserve from transactions with a former controlling party" and also from the exercises of options into shares.

Current ratio by % - at March 31:



On March 31, 2006 the Company had a working-capital deficiency of $162m and a current ratio of 72.5% as compared with $107m and 80.8% on December 31, 2005, respectively.

The increase in the working-capital deficiency stems mostly from declining cash and short-term investments and short-term deferred-tax receivable along with higher current liabilities arising from an increase in deferred revenues from the sale of airline tickets not yet realized.

The working-capital deficiency stems from current liabilities which include two material components: (i) deferred income from the sale of flight tickets and (ii) current maturities of long-term loans. Both components, which are characterized by the business cycle, are included in current liabilities and in fact explain most of the working-capital deficiency.

3. Analysis of business activities

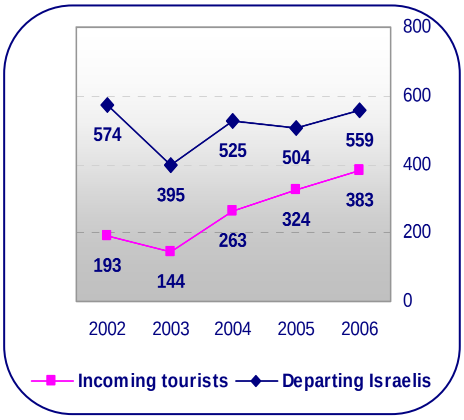
3.1 Market data

Passenger and cargo traffic at BGA	Jan-Mar 2006 in thousands	Jan-Mar 2005 in thousands	change in thousands	%
Incoming tourists *	383	324	59	18%
Departing Israelis *	559	504	55	11%
Cargo import - tons **	32	33	(1)	(2%)
Cargo export - tons **	51	53	(2)	(3%)

(*) Source: the Israeli Bureau of Statistics.

(**) Excluding cargo in transit.

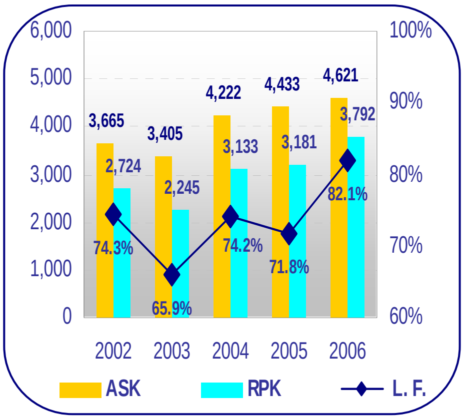
Passenger traffic at BGA Incoming tourists & Departing Israelis, first quarter by year: (In thousands)



3.2 Operating data

	Jan-Mar 2006	Jan-Mar 2005	change
Passenger leg (scheduled and chartered) - in thousands	822	679	21%
RPK (scheduled) - in millions	3,792	3,181	19%
ASK (scheduled) - in millions	4,621	4,433	4%
Load factor (scheduled)	82.1%	71.8%	14%
The Company's market share (scheduled and chartered)	48.3%	46.7%	3%
Cargo, in thousand tons	46	44	5%
RTK - in millions	233	234	(0%)
Weighted flying hours (including leased equipment) - in thousands (*)	41	40	4%
Average man-years (El AL only):			
Permanent	3,659	3,460	6%
Temporary	2,440	2,066	18%
Aircraft in operation - end of period - number of units	35	33	2
Average age of owned fleet at the end of the period - in years	14.5	14.1	0.4

Operating data, first quarter by year: (in millions)



Reading:

Passenger Leg - Flight coupon in one direction.

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

ASK - Available Seat Kilometer - number of seats offered for sale X distance flown.

RTK - Revenue Ton Kilometer - cargo weight in ton X distance flown.

Passenger Load factor - Revenue Passenger Kilometer, expressed as percentage of Available Seat Kilometer.

*Aircraft weighted block hours in terms of Boeing 767/757:

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

These values have been determined on the basis of total expenses incurred for each type of aircraft and used consistently for computing weighted flight hours as an indicator of the volume of aviation activity.

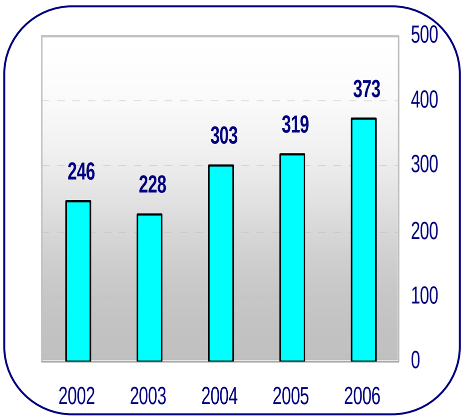
3.3 Profit and loss:

Three-month period ended March 31, 2006 (consolidated):

	Jan - Mar 2006		Jan - Mar 2005		change	
	in thousands US dollars	% of operating revenues	in thousands US dollars	% of operating revenues	in thousands US dollars	%
Operating revenues	372,549	100%	319,423	100%	53,126	17%
Operating expenses	(314,833)	(84.5%)	(273,425)	(85.6%)	(41,408)	15%
Gross profit	57,716	15.5%	45,998	14.4%	11,718	25%
Selling expenses	(41,145)	(11.0%)	(41,091)	(12.9%)	(54)	0%
General and administrative expenses	(22,403)	(6.0%)	(20,607)	(6.5%)	(1,796)	9%
Operating loss before financing, net	(5,832)	(1.6%)	(15,700)	(4.9%)	9,868	(63%)
Financing expenses, net	(6,958)	(1.9%)	(3,351)	(1.0%)	(3,607)	108%
Other incomes, net	314	0.1%	351	0.1%	(37)	(11%)
Income taxes	(11)	(0.0%)	(29)	(0.0%)	18	(62%)
Loss after taxes	(12,487)	(3.4%)	(18,729)	(5.9%)	6,242	(33%)
Company's equity in results of affiliates, net	42	0.0%	266	0.1%	(224)	(84%)
Loss for the period	**(12,445)**	(3.3%)	**(18,463)**	(5.8%)	6,018	(33%)

Major factors affecting the business results for the three-month period ended March 31, 2006 as compared with the corresponding period last year are as follows:

Operating revenues, first quarter by year: (in millions US dollars)

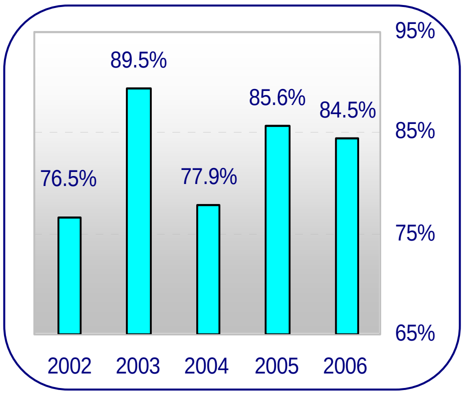


- The higher operating revenues stemmed mainly from an increase in the number of passengers flown as well as a rise in cargo income due to higher cargo quantities flown and an increase in average income per ton/km cargo flown.

- The volume of activity rose over the same quarter last year, as manifested in terms of passenger legs and weighted flight hours. Operating expenses rose mainly due to the noted higher volume of activities, and in addition - an increase in jet-fuel prices, higher aircraft-leasing expenses, increase in aircraft and flight-equipment maintenance expenses and an increase in wages, as detailed below.

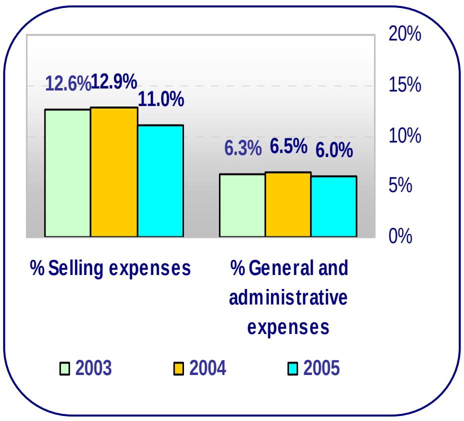
- Average market jet-fuel prices rose during the quarter by an average 27% over the corresponding quarter last year. The Company's jet-fuel expenses rose by 27% from $77.1m to $98.0m, net of hedging rebates totaling $16.0m (same quarter last year - $9.0m). During the quarter jet-fuel expenses constituted 31.1% of total operating expenses as compared with 28.2% in the same quarter last year. The price increases during the quarter added $17.6m to the Company's expenses (net of hedging rebates), with the remaining increase in expenses stemming from higher jet-fuel consumption following the increase in the Company's business activity.

Operating expenses as % of operating revenues, first quarter by year:



- Aircraft and flight-equipment maintenance expenses rose by $7.7m, stemming from the higher activity, fluctuations in timing of engine repairs, higher cost of spare parts and the beginning of payments for an additional engine fleet whose insurance coverage has expired.
- Aircraft-leasing expenses rose by $3.3m, mainly due to the addition of two 737-800 aircrafts.
- General & administrative expenses rose on the heels of higher rental fees paid to the Airports Authority in accordance with its agreements with the Company; nevertheless, their proportion to the first-quarter revenues has declined as compared with the ration in the same quarter last year. Selling expenses have not changed materially while their ratio to revenues has declined during the first quarter as compared to this ratio in the corresponding quarter last year.

Selling expenses & General and administrative expenses as % of operating revenues, first quarter by year:



- Current wages rose, among other reasons, due to an increase in the average workforce, stemming from the higher activity, discontinued deduction of the employees' growth-encouragement component starting February 2005 and the payment of a cost-of-living allowance paid to all the workers in the country. These factors have partly been offset by the shekel's devaluation against the dollar which has reduced the Company's wage expense. As for the effect of the change in the shekel-dollar exchange rate - see item 3.4 below.

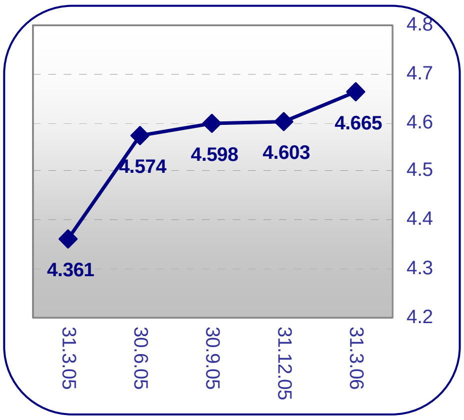
- Higher Libor interest rates have led to an increase in financing expenses, offset by a reduction in total outstanding loans and by higher interest income on bank deposits (due to higher rates and a larger balance of deposits).

3.4 Effect of exchange-rate changes on the Company's liabilities for severance pay (including it's early retirement programs), sick leave and vacation pay

During the first quarter the shekel was devalued by 1.3% against the dollar, as compared with 1.2% in the same quarter last year.

On March 31, 2006 the Company had liabilities totaling $152m in respect of severance pay, retirement programs, sick-leave and vacation pay.

Changes in US dollar exchange rate:



Since most of these liabilities are denominated in shekels while the Company's functional currency is the US dollar, their translation into dollars creates exchange-rate differences stemming from changes in the exchange rate. Such changes are not one-sided thus creating income or expenses which neither affect cash flows nor short-term operating expenses. In order to be able to compare business results over time it is necessary to neutralize these income and expense items. This impact progressively declines along with the State's deposits to the severance-pay fund.

During the first quarter the expenses in respect of this component declined by $1.5m as compared with $2.1m in the same quarter last year.

The following table presents the business results neutralizing the exchange-rate effect on the accrued severance pay, as explained above:

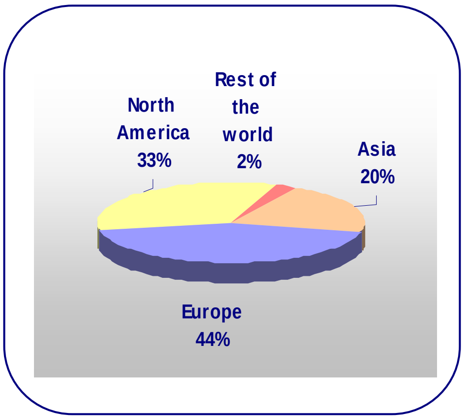
Three-month period ended Mar-31	Before neutralizing the exchange-rate effect on the accrued severance pay 2006	2005	After 2006	2005
	(in thousands US dollars)			
Operating expenses	314,833	273,425	315,780	274,721
Gross profit	57,716	45,998	56,769	44,702
Gross profit rate	15.5%	14.4%	15.2%	14.0%
Selling, general and administrative expenses	63,548	61,698	63,733	61,973
Operating loss before financing expenses	(5,832)	(15,700)	(6,964)	(17,271)
Operating loss rate before financing	(1.6%)	(4.9%)	(1.9%)	(5.4%)
Other expenses, net	314	351	(85)	(193)
Loss for the period	(12,445)	(18,463)	(13,976)	(20,578)
Loss for the period rate	(3.3%)	(5.8%)	(3.8%)	(6.4%)

3.5 Reporting by segments

The following is a summary by geographical segments - consolidated:

Three-month period ended:				
31.03.06 -(unaudited)	North America	Europe	Central Asia & Far East	Rest of the world
	(in millions US dollars)			
operating revenues	122.9	160.3	75.2	8.8
Operating income (loss)	(1.2)	19.3	18.0	2.4
% of operating revenues (loss) *	(1.0%)	12.0%	23.9%	27.1%
31.03.05 -(unaudited)				
operating revenues	105.2	137.1	62.5	7.4
Operating income	2.0	19.6	5.2	2.5
% of operating revenues *	1.9%	14.3%	8.3%	33.2%
Year ended:				
31.12.05 -(audited)				
operating revenues	568.3	710.3	277.1	34.9
Operating income	58.5	166.4	33.8	11.6
% of operating revenues *	10.3%	23.4%	12.2%	33.2%

Operating revenues attributed to geographical segments - January - March 2006:



(*) Excluding unclassified segment expenses (see Note 8 to the interim financial statements).

During the first quarter all segments enjoyed higher revenues over the same period in the previous year while operating income declined in all segments (except for Central Asia and the Far East) due to higher costs (mainly the jet-fuel component). The higher operating income in Central Asia and the Far East stemmed mainly from an increase in the number of passengers, higher load factor rate (in both passenger and cargo aircraft) as well as higher cargo income from passenger aircraft.

4. Seasonal factors

The passenger traffic at BGA is characterized by strong seasonality, with the primary activity taking place during the summer months, (peaking in July-September). The winter months (January-March) are characterized by slow passenger traffic coupled with strong export cargo of agricultural produce to Europe.

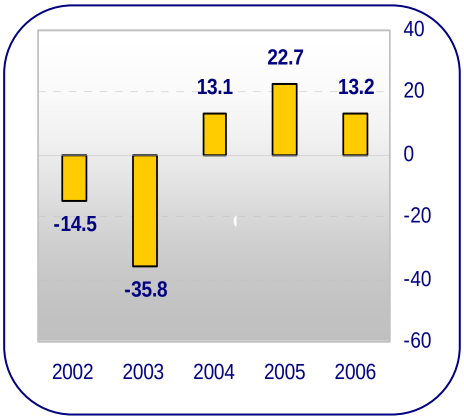
5. Liquidity and financing sources

	Jan-Mar 2006	Jan-Mar 2005	change
	(in thousands US dollars)		
Cash flows from operating activities	13,151	22,675	(9,524)
Cash flows used for investing activities	(26,798)	(12,019)	(14,779)
Cash flows used for financing activities	(7,997)	(5,449)	(2,548)
Net increase (decrease) in cash	(21,644)	5,207	(26,851)

The change in cash flows from operating activities in the first quarter of 2006 compared to the same period last year stemmed mainly from lower accounts payables and higher receivables, mainly offset by a reduction in both the loss for the period and the inventory balance.

Cash flows from operating activities, first quarter by year:

(in millions US dollars)



During the quarter the Company used $38.6m for payments on account of aircraft and fixed assets, spare parts and accessories (as compared with $11.6m in the corresponding period last year) while realizing a net amount of $11.6m in short-term deposits (as compared with the placement of new deposits amounting to a net $0.3m in the corresponding period last year).

In total, the company used $26.8m for its investment activities during the first quarter as compared with $12.0m in the same period last year.

During the quarter the Company repaid long-term loans totaling $6.1m as compared with $5.9m in the corresponding period last year.

In total, the Company used during the quarter $8.0m for financing activities, as compared with $5.4m in the same period last year.

Total cash and cash equivalents as well as short-term investments on March 31, 2006 amounted to $173.5m as compared with $206.8m on December 31, 2005 (March 31, 2005 - $158.8m).

During the reported period the State deposited $0.4m to the employees' severance-pay fund, in accordance with the terms of the prospectus, while the Company also deposited $0.3m (received from an exercise of options (Series 1)) to the employee's severance-pay fund.

6. Quality reporting concerning exposure to market risks and methods used for managing them

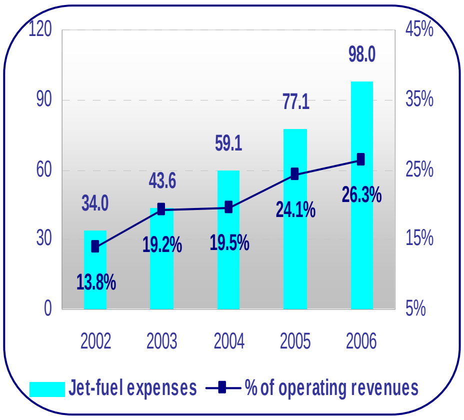
6.1 The Company's policy for managing market risks, the responsibility for managing them, means of supervision and policy implementation

The board's Committee for Managing Marker Risks, headed by the Chairman of the Finance Committee, Mr. Nadav Palti, is responsible for establishing a policy to cover against existing risks while the CFO is responsible for carry this policy out and reporting to the committee.

The Committee determines future frameworks of jet-fuel consumption which are to be covered by hedging transactions while examining, from time to time, the need to invest in derivatives in an effort to reduce interest rate and exchange-rate risks. The Company's policy regarding the management of market risks and the related supervision means did not change during the reported period, as described in the 2005 annual directors' report and in the notes to the 2005 annual financial statements (see notes 6.2, 6.3 and 6.4 below).

Total Jet-fuel expenses and % of operating revenues, first quarter by years:

(in millions US dollars)



6.2 Hedging jet-fuel prices

The following is an outline of the hedging transactions (recognized for accounting purposes) outstanding on March 31, 2006:

	Type of transaction	Period	Transaction's currency	Fair value in thousand US dollars
HJFP	Financial instruments	Up to One year	US dollar	44,661
HJFP	Financial instruments	Over One year	US dollar	3,340

For more details see Note 20b.1 to the 2005 annual financial statements.

6.3 Hedging loan interest rates

During 2004 and 2005 the Company entered, along with banks in Israel, into several swap transactions for hedging part of its exposure to changes in interest rates. No additional transactions were carried out during the first quarter of 2006. Some of the abovementioned financial instruments, whose fair value on March 31, 2006 was $2.2m, are not recognized for accounting purposes and presented in the balance sheet as "receivables and other current assets". Other agreements are recognized for accounting purposes. Following these transactions, about 74% of the outstanding loans on March 31, 2006 were at fixed rates (for five years). It should be noted that part of the above hedging transactions at that date were ineffective since the interest rate had passed the exit point established with the banks.

For additional details see Note 20b.2 to the 2005 annual financial statements.

6.4 Hedging exchange rates

During the reported period the Company carried out several financial transactions (not recognized for accounting purposes) designed to protect from a dollar decline against the shekel. The fair value of these transactions on March 31, 2006 amounted to $0.2m and presented in the financial statements within "receivables and other current assets".

7. Linkage

Consolidated linkage basis at March 31, 2006:

	In, or linked to the US dollar	In Israeli currency	In, or linked to the euro	In, or linked to the other currencies	Non-monetary items	Total
	(in thousands US dollars)					
Assets						
Cash and cash equivalents	47,615	19,674	1,430	3,566	-	72,285
Short-term investments	101,238		-	-	-	101,238
Trade accounts receivable	131,290	87	13,465	14,608	-	159,450
Receivables and other current assets	15,650	9,546	1,292	1,701	26,729	54,918
Deferred income taxes	-	-	-	-	21,758	21,758
Inventory	-	-	-	-	17,480	17,480
Long-term bank deposits	-	1,751	-	-	-	1,751
Investment in another company	-	-	-	-	1,877	1,877
Investees	1,554	-	-	-	677	2,231
Fixed assets	53,189	-	-	-	1,119,722	1,172,911
Other assets	-	-	-	-	2,491	2,491
	350,536	**31,058**	**16,187**	**19,875**	**1,190,734**	**1,608,390**
Liabilities & Equity						
Short-term borrowings	(73,271)	-	(534)	(40)	-	(73,845)
Trade accounts payable	(87,334)	(24,292)	(14,331)	(10,199)	-	(136,156)
Payables and other current liabilities	(113,423)	(85,607)	(1,368)	(756)	(178,080)	(379,234)
Long-term loans	(619,493)	-	-	-	-	(619,493)
Accrued severance pay, net	(30,235)	(80,494)	(5,283)	(1,434)	-	(117,446)
Deferred income taxes	-	-	-	-	(21,333)	(21,333)
Other long-term liabilities	(1,671)	-	-	-	-	(1,671)
Shareholders' equity	-	-	-	-	(259,212)	(259,212)
	(925,427)	**(190,393)**	**(21,516)**	**(12,429)**	**(458,625)**	**(1,608,390)**
Monetary assets, net of monetary liabilities (monetary liabilities, net of monetary assets)	**(574,891)**	**(159,335)**	**(5,329)**	**7,446**	**732,109**	**-**

Consolidated linkage basis at March 31, 2005:

	In, or linked to the US dollar	In Israeli currency	In, or linked to the euro	In, or linked to the other currencies	Non-monetary items	Total
	(in thousands US dollars)					
Assets						
Cash and cash equivalents	60,113	1,678	4,666	3,397	-	69,854
Short-term investments	86,953	-	-	1	-	86,954
Trade accounts receivable	123,188	413	6,915	14,106	-	144,622
Receivables and other current assets	13,089	3,335	1,711	424	16,183	34,742
Inventory	-	-	-	-	10,324	10,324
Long-term bank deposits	239	1,762	-	-	-	2,001
Investment in another company	-	-	-	-	1,832	1,832
Investees	1,554	-	-	-	7,756	9,310
Fixed assets	4,172	-	-	-	1,168,596	1,172,768
Other assets	-	-	-	-	4,112	4,112
	289,308	**7,188**	**13,292**	**17,928**	**1,208,803**	**1,536,519**
Liabilities & Equity						
Short-term borrowings	(79,429)	-	(42)	(43)	-	(79,514)
Trade accounts payable	(89,713)	(22,326)	(13,944)	(11,372)	-	(137,355)
Payables and other current liabilities	(84,199)	(89,312)	(6,572)	(2,732)	(139,536)	(322,351)
Long-term loans	(675,313)	-	-	-	-	(675,313)
Accrued severance pay, net	(14,899)	(105,708)	(5,537)	(1,314)	-	(127,458)
Other long-term liabilities	(3,844)	(231)	-	-	-	(4,075)
Shareholders' equity	-	-	-	-	(190,453)	(190,453)
	(947,397)	**(217,577)**	**(26,095)**	**(15,461)**	**(329,989)**	**(1,536,519)**
Monetary assets, net of monetary liabilities (monetary liabilities, net of monetary assets)	**(658,089)**	**(210,389)**	**(12,803)**	**2,467**	**878,814**	**-**

Consolidated linkage basis at December 31, 2005:

	In, or linked to the US dollar	In Israeli currency	In, or linked to the euro	In, or linked to the other currencies	Non-monetary items	Total
	(in thousands US dollars)					
Assets						
Cash and cash equivalents	78,279	11,345	1,503	2,802	-	93,929
Short-term investments	111,841	993	-	-	-	112,834
Trade accounts receivable	99,877	45	10,331	13,593	-	123,846
Receivables and other current assets	19,592	6,085	232	1,042	21,733	48,684
Deferred income taxes	-	-	-	-	46,698	46,698
Inventory	-	-	-	-	22,445	22,445
Long-term bank deposits	-	1,779	-	-	-	1,779
Investment in another company	-	-	-	-	1,878	1,878
Investees	1,554	-	-	-	635	2,189
Fixed assets	26,763	-	-	-	1,137,002	1,163,765
Other assets	-	-	-	-	4,671	4,671
	337,906	**20,247**	**12,066**	**17,437**	**1,235,062**	**1,622,718**
Liabilities & Equity						
Short-term borrowings	(75,713)	-	-	-	-	(75,713)
Trade accounts payable	(95,380)	(28,412)	(21,398)	(9,856)	-	(155,046)
Payables and other current liabilities	(103,547)	(84,357)	(10)	(1,058)	(135,574)	(324,546)
Long-term loans	(627,363)	-	-	-	-	(627,363)
Accrued severance pay, net	(29,332)	(84,762)	(5,058)	(1,374)	-	(120,526)
Deferred income taxes	-	-	-	-	(46,300)	(46,300)
Other long-term liabilities	(2,215)	-	-	-	-	(2,215)
Shareholders' equity	-	-	-	-	(271,009)	(271,009)
	(933,550)	**(197,531)**	**(26,466)**	**(12,288)**	**(452,883)**	**(1,622,718)**
Monetary assets, net of monetary liabilities (monetary liabilities, net of monetary assets)	**(595,644)**	**(177,284)**	**(14,400)**	**5,149**	**782,179**	**-**

8. Issue to which the independent auditors drew attention in their review letter on the interim financial statements

In their review letter on the interim financial statements as of March 31, 2006, the independent auditors drew attention to note 7 concerning the Company's exposure to lawsuits approved as class action. Although this topic does not constitute a qualification, such notation is required due to its potential material impact on the Company.

9. Disclosure pertaining to consent for peer review

On July 28, 2005 the Israeli Securities Authority published a guideline in accordance with Section 36a of the Securities Law, 1968, concerning disclosure of consent to conduct a survey by colleagues, aimed, pursuant to the abovementioned guideline, to trigger a control procedure over the work of the independent auditors and examine the fulfillment of the procedures required during their audit work, for the purpose of maintaining an advanced capital market. On March 29, 2006 the board approved the granting of this consent.

10. Subsequent event

As for event taking place subsequent to the balance-sheet date (increasing the number of options) - see Note 9 to the interim financial statements.

Haim Romano	**Prof. Israel (Izzy) Borovich**
Chief Executive Officer	**Chairman of the Board**

May 23, 2006

FINANCIAL STATEMENTS
AS OF MARCH 31, 2006

SECTION C

FINANCIAL STATEMENTS

EL AL ISRAEL AIRLINES LTD.
CONDENSED CONSOLIDATED
INTERIM FINANCIAL STATEMENTS
AS OF MARCH 31, 2006
(unaudited)

EL AL ISRAEL AIRLINES LTD.
CONDENSED CONSOLIDATED
INTERIM FINANCIAL STATEMENTS
AS OF MARCH 31, 2006
(unaudited)

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

Gentlemen:

Review of the unaudited condensed consolidated interim financial statements at March 31, 2006 and for the three-month period then ended

Pursuant to your request we have reviewed the accompanying condensed consolidated interim balance sheet of El Al Israel Airlines Ltd. ("the Company") at March 31, 2006 and the condensed consolidated interim statements of operations, changes in shareholders' equity and cash flows for the three-month period then ended.

Our review has been performed in accordance with procedures prescribed by the Institute of Certified Public Accountants in Israel. These procedures included, among other things: reading the aforementioned financial statements, reading the minutes of the shareholders' meetings and the meetings of the board of directors and its committees, and making inquiries with persons responsible for the financial and accounting affairs.

We have been furnished reports of other accountants relating to the review of interim condensed financial statements of subsidiaries whose assets constitute 1% of total assets included in the condensed interim consolidated balance sheet and whose revenues constitute 0.3% of total revenues included in the condensed interim consolidated statements of operations for the three-month period ended March 31, 2006.

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

In performing our review, which included the reading of the reports of other accountants, nothing came to our attention indicating that material modifications are required to these interim financial statements for them to be deemed prepared in conformity with generally accepted accounting principles and in accordance with Paragraph D of the Israeli Securities Regulations (Periodic and Immediate Financial Statements), 1970.

We draw attention to Note 7 to the interim financial statements concerning exposure to lawsuits approved as class action.

Respectfully,

Brightman Almagor & Co.
Certified Public Accountants
A Member Firm of Deloitte Touche Tohmatsu

Tel Aviv, May 23, 2006

EL AL ISRAEL AIRLINES LTD.
CONDENSED CONSOLIDATED INTERIM BALANCE SHEETS

	March 31,		December 31,
	2 0 0 6	2 0 0 5	2 0 0 5
	(unaudited)		(audited)
	(in thousand US dollars)		
Current assets			
Cash and cash equivalents	72,285	69,854	93,929
Short-term investments	101,238	86,954	112,834
Trade accounts receivable	159,450	144,622	123,846
Receivables and other current assets	54,918	34,742	48,684
Deferred income taxes	21,758	-	46,698
Inventory	17,480	10,324	22,445
	427,129	346,496	448,436
Investments			
Long-term bank deposits	1,751	2,001	1,779
Investment in another company	1,877	1,832	1,878
Investees	2,231	9,310	2,189
	5,859	13,143	5,846
Fixed assets	1,172,911	1,172,768	1,163,765
Other assets	2,491	4,112	4,671
	1,608,390	1,536,519	1,622,718

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

EL AL ISRAEL AIRLINES LTD.
CONDENSED CONSOLIDATED INTERIM BALANCE SHEETS

	March 31, 2006	March 31, 2005	December 31, 2005
	(unaudited)	(unaudited)	(audited)
	(in thousand US dollars)		
Current liabilities			
Short-term borrowings and current maturities	73,845	(*) 79,514	75,713
Trade accounts payable	136,156	137,355	155,046
Payables and other current liabilities	379,234	(*) 322,351	324,546
	589,235	539,220	555,305
Long-term liabilities			
Long-term loans from financial institutions	619,493	675,313	627,363
Accrued severance pay, net	117,446	127,458	120,526
Deferred income taxes	21,333	-	46,300
Other long-term liabilities	1,671	4,075	2,215
	759,943	806,846	796,404
Total liabilities	1,349,178	1,346,066	1,351,709
Shareholders' equity			
Share capital	131,525	131,247	131,318
Premium on shares	900	802	826
Capital reserve from transactions with a former controlling party	299,486	299,119	299,119
Differences from the translation of investees' financial statements	-	2,128	-
Accumulated deficit	(172,699)	(242,843)	(160,254)
	259,212	190,453	271,009
	1,608,390	1,536,519	1,622,718

(*) Reclassified.

Prof. Israel (Izzy) Borovich	Haim Romano	Nissim Malki
Chairman of the Board	**Chief Executive Officer**	**Chief Financial Officer**

Approval date of the financial statements - Ben Gurion Airport, May 23, 2006

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

EL AL ISRAEL AIRLINES LTD.
CONDENSED CONSOLIDATED INTERIM STATEMENT OF OPERATIONS

	Three-month period ended March 31,		Year ended December 31,
	2006	2005	2005
	(unaudited)		(audited)
	(in thousand US dollars)		
Operating revenues	372,549	319,423	1,619,469
Operating expenses	314,833	273,425	1,243,198
Gross profit	57,716	45,998	376,271
Selling expenses	41,145	41,091	198,591
General and administrative expenses	22,403	20,607	88,758
	63,548	61,698	287,349
Operating income (loss) before net financing expenses	(5,832)	(15,700)	88,922
Net financing expenses	6,958	3,351	20,606
Operating income after net financing expenses	(12,790)	(19,051)	68,316
Other income (expenses), net	314	351	(4,519)
Pre-tax income (loss)	(12,476)	(18,700)	63,797
Income taxes	11	29	304
Income (loss) after income taxes	(12,487)	(18,729)	63,493
Company's equity in earnings of affiliates, net	42	266	633
Net income (loss) for the period	(12,445)	(18,463)	64,126
Basic earnings (loss) per share - in dollars	(0.03)	(*) (0.05)	(*) 0.16
Number of shares used in the computation of basic EPS (in thousands)	400,364	399,401	399,633
Fully diluted earnings per share - in dollars	-	-	0.13
Number of shares used in the computation of fully diluted EPS (in thousands)	-	-	495,721

(*) Restated - see Note 1.3.1.

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

EL AL ISRAEL AIRLINES LTD.
INTERIM STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

	Share capital	Premium On shares	Capital reserve(*)	Differences (**)	Accumulated deficit	Total
			(in thousand US dollars)			
Three-month period ended March 31, 2006 (unaudited):						
Balance - January 1, 2006	131,318	826	299,119	-	(160,254)	271,009
Receipts on account of government of Israel debt	-	-	367	-	-	367
Exercise of options into shares	207	74	-	-	-	281
Loss for the period	-	-	-	-	(12,445)	(12,445)
Balance - March 31, 2006	131,525	900	299,486	-	(172,699)	259,212
Three-month period ended March 31, 2005 (unaudited):						
Balance - January 1, 2005	130,940	699	273,328	2,232	(224,380)	182,819
Differences (**)	-	-	-	(104)	-	(104)
Receipts on account of government-of Israel debt	-	-	25,791	-	-	25,791
Exercise of options into shares	307	103	-	-	-	410
Loss for the period	-	-	-	-	(18,463)	(18,463)
Balance - March 31, 2005	131,247	802	299,119	2,128	(242,843)	190,453
Year ended December 31, 2005 (audited):						
Balance - January 1, 2005	130,940	699	273,328	2,232	(224,380)	182,819
Differences (**)	-	-	-	(104)	-	(104)
Realization of an investee	-	-	-	(2,128)	-	(2,128)
Receipts on account of government-of Israel debt	-	-	25,791	-	-	25,791
Exercise of options into shares	378	127	-	-	-	505
Net income for the period	-	-	-	-	64,126	64,126
Balance - December 31, 2005	131,318	826	299,119	-	(160,254)	271,009

(*) Arising from transactions with a former controlling party.
(**) Arising from the translation of investees' financial statements.

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

EL AL ISRAEL AIRLINES LTD.
CONDENSED CONSOLIDATED INTERIM STATEMENT OF CASH FLOWS

	Three-month period ended March 31,		Year ended December 31,
	2006	2005	2005
	(unaudited)		(audited)
	(in thousand US dollars)		
CASH FLOWS - OPERATING ACTIVITIES			
Net income (loss) for the period	(12,445)	(18,463)	64,126
Adjustments required to present net cash flows provided by operating activities (Appendix A)	25,596	(**) 41,138	119,493
Net cash provided by operating activities (*)	13,151	22,675	183,619
CASH FLOWS - INVESTING ACTIVITIES			
Investment in other assets	-	(429)	(1,485)
Additions to fixed assets (includes payments on account of aircraft purchases	(38,606)	(11,586)	(82,822)
Proceeds from disposition of fixed assets	209	123	954
Decrease (increase) in short-term deposits, net	11,594	(306)	(26,428)
Investment in long-term deposits	(68)	(94)	(368)
Realization of long-term deposits	71	26	678
Investment in supplier deposits	-	-	(121)
Redemption of supplier deposits	-	2	130
Dividend received, less investees' earnings, net	-	94	-
Proceeds from realization of investments in investess	-	-	13,656
Decrease in investments and loans to investees, net	2	151	151
Net cash used for investing activities	(26,798)	(12,019)	(95,655)
CASH FLOWS - FINANCING ACTIVITIES			
Repayment of long-term loans from financial institutions	(5,625)	(5,387)	(77,160)
Repayment of another long-term loan	(515)	(501)	(2,017)
Proceeds from exercise of options into shares	281	410	505
Receipt of long-term loans from financial institutions	-	-	14,169
Net increase (decrease) in short term borrowings	(2,138)	(*) 29	5,821
Net cash used for financing activities	(7,997)	(5,449)	(58,682)
Net increase (decrease) in cash and cash equivalents	(21,644)	5,207	29,282
Cash and cash equivalents at the beginning of the period	93,929	64,647	64,647
Cash and cash equivalents at the end of the period	72,285	69,854	93,929
(*) Without depositing the issuance proceeds in the severance-pay fund for covering past liabilities.	13,410	21,029	184,154

(**) Reclassified.

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

EL AL ISRAEL AIRLINES LTD.
CONDENSED CONSOLIDATED INTERIM STATEMENT OF CASH FLOWS

	Three-month period ended March 31,		Year ended December 31,
	2006	2005	2005
	(unaudited)		(audited)
	(in thousand US dollars)		
Appendix A - Adjustments required to present net cash flows provided by operating activities			
Income and expenses not involving cash flows:			
Depreciation and amortization (including disposals of accessories, components no longer in use and consumption of supplies)	29,501	27,867	108,269
Adjustment in the value of long- term deposits	27	22	108
Company's equity in earnings of affiliates, net of dividends received (**)	(42)	-	(273)
Deferred income taxes	(27)	-	(77)
Decrease in accrued severance pay, net	(1,699)	(2,900)	(10,298)
Capital gains from disposition of fixed assets, net	(67)	(94)	(590)
Capital gain from realization of an investment in an investee	-	-	(8,297)
Adjustment in value of supplier deposits	1	2	(51)
Changes in assets and liabilities:			
Increase in trade accounts receivable	(35,604)	(33,442)	(12,667)
Increase in receivables and other current assets	(6,234)	(1,625)	(16,087)
Decrease (increase) in inventory	4,966	(849)	(12,970)
Increase (decrease) in trade accounts payable	(18,891)	1,229	18,920
Increase in payables and other current assets	53,673	(*) 50,904	53,566
Increase (decrease) in other long-term liabilities	(8)	24	(60)
	25,596	41,138	119,493

(*) Reclassified.

(**) Dividends received	-	360	360

Appendix B - Non-cash transactions

Government of Israel deposits to the employees' severance-pay fund	367	25,791	25,791

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

NOTE 1 - REPORTING RULES AND ACCOUNTING POLICY

1.1 The interim financial statements have been prepared in a condensed format, in conformity with the accounting principles generally accepted for the preparation of interim financial statements, as prescribed by Standard No.14 of the Israeli Accounting Standards Board and the Israeli Securities Regulations (Preparation of Periodic and Immediate Financial Statements), 1970. The significant accounting policies adopted in the Company's 2005 audited annual financial statements have been consistently applied during the reported period. These interim financial statements should be read in conjunction with the 2005 annual financial statements, including their accompanying notes.

1.2 Changes in the consumer-price index (CPI) and the Dollar-Euro/Nis exchange rate:

	March 31		December 31
	2006	**2005**	**2005**
CPI (in points)	186.12	179.66	185.05
$/NIS	4.665	4.361	4.603
$/€	0.824	0.772	0.845

	Three-month period ended March 31		Year ended December 31
Change - %	**2006**	**2005**	**2005**
CPI (in points)	0.6	(0.6)	2.4
$/NIS	1.3	1.2	6.8
$/€	(2.5)	5.3	15.3

1.3 Initial implementation of new accounting standards

1.3.1 Accounting Standard No.21 - Earnings per share

In February 2006 the Israeli Accounting Standards Board issued Accounting Standard No. 21 ("Earnings per Share"), which went into effect on January 1, 2006. Upon the introduction of this standard, Opinion No. 55 of the Institute of Certified Public Accountants in Israel on EPS was superseded. The standard establishes that an entity is to compute its basic EPS in regard to income or loss attributable to holders of ordinary shares of the reporting entity, and that the entity shall compute its basic EPS with respect to any income or loss from continuing operations attributable to holders of ordinary shares. Basic EPS are to be computed by dividing income or loss attributed to holders of ordinary shares of the reporting entity (numerator), by the weighted average of the outstanding ordinary shares (denominator) during the period. In its computation of diluted EPS the entity must adjust its income or loss attributable to holders of ordinary shares and the weighted average of the outstanding shares for the effects of all the dilutive potential ordinary shares. According to the standard, which will apply to financial statements covering periods starting January 1, 2006 and thereafter, its provisions are to be applied retroactively in respect of comparative EPS data relating to prior periods. Pursuant to the standard's provisional rules, the Company restated its EPS dada pertaining to prior periods and, consequently, its basic EPS for 2005 rose by $0.03 while the loss for the three-month period ended March 31, 2005 increase by $0.01 per share. The Company fully diluted EPS for 2005 has not changed.

NOTE 1 - REPORTING RULES AND ACCOUNTING POLICY (Cont.)

1.3 Initial implementation of new accounting standards

1.3.2 **Accounting Standard No. 22 - Financial Instruments Disclosure and Presentation:**

At the end of July 2005 the Israeli Accounting Standards Board published Accounting Standard No. 22 ("Financial Instruments: Disclosure and Presentation"), which went into effect on January 1, 2006, establishing the rules for presentation of financial instruments in the financial statements and outlining the disclosure required in respect thereof. The presentation requirements pertain to the classification of financial instruments as financial assets, financial liabilities or capital instruments. It also addresses the classification of related interest, dividends, losses and profits and to the circumstances under which financial assets and liabilities are to be offset. The standard cancelled, upon its introduction, Opinion No.53 ("Accounting Treatment of Convertible Liabilities") and Opinion no. 48 ("Accounting Treatment of Options"). The effect of the standard on the Company's financial position and results of operations has not been material.

1.3.3 **Accounting Standard No.24 - Stock-Based Payment**

In September 2005 the Israeli Accounting Standards Board published Accounting Standard No. 24 ("Stock-Based Payment"), which went into effect on January 1, 2006, requiring the recognition in financial statements of share-based payments, including transactions with employees or other parties to be settled in cash, other assets or equity instruments; consequently, among other things, expenses incurred in respect of share grants and options given to employees over the vesting period of those grants based on the fair value of each grant at the time granted. The standard establishes measuring rules as well as specific requirements pertaining to transactions with share-based payment which are settled with equity instruments and payment transactions which provide each one of the parties a choice between settling the transaction in cash or in equity instruments. The standard also establishes various disclosure requirements in regard to the share-based payments.

As for stock-based payment transactions settled in cash, the standard requires measuring the acquired merchandise or services and the created liability based on the latter's fair value. Until the liability is paid, its fair should be re-measured at any reporting date and when paying the liability, with any changes therein recognized as income or loss in the period. As for the standard's implementation in regard to the employee options plan on which it was decided during the reported period starting the second quarter of 2006 - see Note 6.3.

NOTE 1 - REPORTING RULES AND ACCOUNTING POLICY (Cont.)

1.3 Initial implementation of new accounting standards (Cont.)

1.3.4 Accounting Standard No.25 - Revenues

In February 2006 the Israeli Accounting Standard Board published Accounting Standard No.25 ("Revenues"), which went into effect on January 1, 2006, establishes rules for the recognition, measurement and presentation of revenues arising from the sale of goods, rendering of services and use by others of entity assets yielding interest, royalties and dividends. The standard states that an entity should measure its revenues based on the fair value of the proceeds received and/or entitled to. An entity which had not presented its revenues in the past based on the standard's requirement in regard to reporting in gross amounts (the gross amount billed to the customer) or net (the amount billed less the payment made to the supplier of goods or services) is required to retroactively implement the standard's provisions in respect of the entire income in all of the reported periods as comparative figures in the financial statements covering periods beginning January 1, 2006.

Assets and liabilities included in the balance sheet on December 31, 2005 in amounts different than those recognized before this standard's implementation will be adjusted on January 1, 2006 to the amounts recognized based on this standard, with the effect of this adjustment recognized as a cumulative effect of an accounting change at the beginning of the period.

The new standard has had no effect on the Company's financial statements.

NOTE 2 - GENERAL

On January 16, 2006 the Minister of Tourism ("the Minister") announced his decision to comply with the request of Israir Aviation and Tourism Ltd., ("Israir") and appoint it as the State of Israel's additional designated carrier on the Tel Aviv - New York route and, accordingly expand its commercial license. Israir will now be licensed to carry out scheduled flights over a 24-month period and it was noted in the decision that "during this period the Minister will examine the ramifications arising from the addition of a designated carrier as well as additional relevant considerations applicable to this route".

The Company's management believes that the Minister's decision violates the authorities' commitment given to the Company before its privatization on the basis of a government resolution (subsequently approved by the High Court of Justice) and that there is no legal and/or economic justification to this departure from this commitment. Accordingly, on January 29, 2006, the Company filed a motion with the High Court of Justice, asking the court to establish that the Minister's decision lacked legal grounds and should thus be revoked. On February 23, 2006 the court rejected this motion, noting that its reasons would be published separately. The reasons have not yet been published to date.

NOTE 3 - FIXED ASSETS

During the reported period the Company paid $27.4m to the Boeing Corporation on account of two ordered 777-200 plus $1.5m paid for the option to order ten 787 aircraft in the future.

NOTE 4 - SEASONAL FACTORS

The passenger traffic at Ben-Gurion Airport is characterized by strong seasonality, with the prime activity taking place during the summer months, peaking in July-September. The winter months (January-March) are characterized by slow passenger traffic, but strong export of agricultural produce to Europe.

NOTE 5 - ACCRUED SEVERANCE PAY, NET

During the reported period the Government of Israel deposited a total of $367,000 to the severance-pay fund of the eligible employees, in respect of the proceeds it had received from the exercise of options and sale of Company shares to the Employees' Company. These deposits, which were made within the framework of the Company's agreement with the Government and the employees, were recorded to "capital reserve from transactions with the former controlling party".

As for the Company's deposits of proceeds from the exercise of options (Series 1) to the severance-pay fund - see Note 6.1.

NOTE 6 - SHARE CAPITAL AND PREMIUM

6.1 During the three-month period ended March 31, 2006, the public exercised 953,428 options (Series 1) into an identical number of Company ordinary shares of NIS 1.00 par-value each. The proceeds received by the Company from this exercise amounted to $281 thousand and were deposited to the eligible employees' severance-pay fund.

6.2 On March 23, 2006 the Company's General Meeting ratified an increase of NIS 54,279,453 in the Company's authorized share capital, bringing the Company's total to NIS 550,000,001, divided into one special State share of NIS 1.00 par value and 550,000,000 registered-in-name par-value ordinary shares of NIS 1.00 each.

6.3 On February 26, 2006 the Company's board of directors adopted an employee and officer options plan of 17,092,129 options exercisable into an identical number of ordinary shares of NIS 1.00 par value each, subject to adjustments. The board will be authorized to increase this number of options from time to time. Concurrently, the board also ratified the allotment of NIS 17,092,129 options to 50 recipients, including 10 officers and 40 other managers. The officers' allotment, which has also been approved ratified by the audit committee on February 26, 2006, is subject to the approval of the General Meeting for increasing the Company's authorized share capital. This approval was granted on March 23, 2006, with the allotment taking place on that date. These options, which were allotted within the framework of a capital-gains track with a trustee in accordance with Section 102 of the Income Tax Ordinance, will not register for trade on a stock exchange but the shares stemming from their exercise will. The options will be fully vested and available for exercise in equal installments over a four-year period starting January 1, 2007 (one-quarter of the options will be vested during each year), so long as the recipient is still employed by the Company or provides services on vesting date. Unexercised options will expire at the end of three years following vesting date. Each option's theoretical price (i.e., an amount not actually paid by the employee) will be NIS 2.9733. Upon exercise, the employee would be eligible to receive a number of shares equaling the difference between the exercise share (an ordinary share's closing price of on the Tel Aviv Stock Exchange on exercise-notice date) and the theoretical exercise price (the later subject to customary adjustments made upon dividend distribution and changes in a company's capital structure).

NOTE 6 - SHARE CAPITAL AND PREMIUM

6.3 (Cont.)

According to the provisions of Accounting Standard No. 24 ("Stock-Based Payment") of the Israeli Accounting Standards Board, the Company would record option-granting expenses based on their economic value and computed by the Black & Scholes model. The computation of the option's value has been made based on the program's terms and subject to the following assumptions:

- The share price equals market closing price on March 23, 2006 (NIS 3.837).
- Exercise price equals 85% of share price on February 26, 2006 (NIS 2.973).
- The estimated exercise period of each batch has been computed by the average between each batch's vesting period and the expiration date.
- The standard deviation has been computed by the daily yield of the share's market price over the estimated exercise period of each batch (as detailed above). A maximal standard deviation was taken (from the registration of the Company's shares for trade after having neutralized the first trading day) in respect of batches whose life expectancy is longer than the period during which the Company's share is traded.
- Discount rate -the yield on unlinked debentures ("Shachar") applicable to each batch's estimated life expectancy.

Based on the above assumptions, the Company would bear a total of NIS 29,894 thousand ($6.4m) in respect of this program, reflecting - based on the Black & Scholes model - an average option price of NIS 1.75.

As for event subsequent to the balance-sheet date - see Note 9.

NOTE 7 - CONTINGENT LIABILITIES

The following two lawsuits (filed in previous years) were approved by the court in previous years as class action:

7.1 In October 1998, a lawsuit for NIS 230.4m ($49m on the balance-sheet date) was filed in the Nazareth District Court against the Company along with a request to recognize it as a class action. The claim alleged airline ticket over-pricing by travel agents using improper exchange rates. In 2002 the court approved the request as class action for the Consumer Protection Law purposes. The Company filed a request to be permitted to appeal to the Supreme Court. In the opinion of management, based on the advice of legal counsel, it is not possible at this stage to assess the outcome of this challenge to the decision to treat the case as a class action and of the claim itself should the appeal not be approved. No provision has been included in these financial statements in respect thereof.

NOTE 7 - CONTINGENT LIABILITIES (Cont.)

7.2 A lawsuit for NIS 21.7m ($4.7m on the balance-sheet date) was filed in September 1999 with the Tel Aviv District Court against the Company, the Airports Authority and Ophir Tours (a travel agency), together with a request for recognition as a class action. The plaintiff alleges that the travel agent charged travel tax at a rate above the legal limit, which is the shekel's representative exchange rate. In 2002 the court approved the request for class action under Regulation 29 of the civil law. The Company filed a request to be permitted to appeal to the Supreme Court.

In October 2005 the Supreme Court ruled in the case of A.S.T that a class action would strictly emanate from specific legislations and that it is not available under Regulation 29 of the civil code. Accordingly, the parties were request by the court to submit their motions on how to continue with the proceedings. The plaintiff informed the court that she wanted to continue proceedings under the Consumer Protection Law, which had not approved by the district court. The Supreme Court has not yet ruled on this matter. Based on the advice of its legal counsel management believes that - at this stage - it is not possible to assess the outcome of this appeal and the claim itself. No provision has been included in these financial statements in respect thereof.

NOTE 8 - OPERATING SEGMENTS

Geographical segments - consolidated	North America	Europe	Central Asia & Far East	Rest of the world	Total
	(in thousand US dollars)				
Three-month period ended March 31, 2006 (unaudited)					
Revenues -					
Segment revenues	122,870	160,316	75,209	8,840	367,235
Revenues not allocated by segment					5,314
Total revenues					372,549
Operating income -					
Operating income (loss), by segment	(1,227)	19,285	18,003	2,392	38,453
Net corporate expenses					(44,285)
Operating loss, before financing expenses					(5,832)
Three-month period ended March 31, 2005 (unaudited)					
Revenues -					
Segment revenues	105,243	137,055	62,533	7,443	312,274
Revenues not allocated by segment					7,149
Total revenues					319,423
Operating income -					
Operating income by segment	2,034	19,578	5,171	2,468	29,251
Net corporate expenses					(44,951)
Operating loss, before financing expenses					(15,700)

NOTE 8 - OPERATING SEGMENTS

Geographical segments - consolidated	North America	Europe	Central Asia & Far East	Rest of the world	Total
	(in thousand US dollars)				
Year ended December 31, 2005 (audited)					
Revenues -					
Segment revenues	568,289	710,265	277,101	34,853	1,590,508
Revenues not allocated by segment					28,961
Total revenues					1,619,469
Operating income -					
Operating income by segment	58,501	166,379	33,765	11,555	270,200
Net corporate expenses					(181,278)
Operating income, before financing expenses					88,922

NOTE 9 - SUBSEQUENT EVENT

On May 23, 2006 the Company's board of directors decided to increase the number of options pursuant to the options program designed to compensate officers and employees (as explained in Note 6.3 above) by an additional 3,000,000 options ("the Program"), which will exercisable into up to 3,000,000 Company ordinary shares of NIS 1.00 par value each.

The board appointed the Human Resources and Appointments Committee as the Program's manager, also empowering it to allot these options to Company officers in accordance with board-established criteria.

The option's theoretical exercise price will equal 85% of an ordinary share's average closing price on the Tel Aviv Stock Exchange during the 30 trading days preceding the Program manager's decision concerning the allotment, except for those serving as vice president or division manager on March 23, 2006 and who had not received any option pursuant to the allotment decision of March 2006, in respect of a which a theoretical exercise price of NIS 2.9733 had been established.