Translation of the Hebrew Language financial statements

EL AL ISRAEL AIRLINES LTD.

FINANCIAL STATEMENTS

AS OF JUNE 30, 2006

(unaudited)

CONTENTS

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 June 30, 2006, the market prices of jet fuel rose on the average, by approximately 25% relative to the corresponding period last year. During the quarterly period, fuel expenses represented approximately 27% of total revenues (approximately 23% of total revenues during the second quarter of the year 2005). The Company estimates that the continuation of the trend of increasing jet fuel prices will have a significant effect on its financial results for the year 2006 (see the update to Section 9.16 below). See Section 6.2 to the Directors' Report for further details.

To Section 6.4- currency rate fluctuations

As of June 30, 2006, there had been a decrease of approximately 3.5% in relation to December 31, 2005, in the rate of exchange of the U.S. dollar vis-à-vis the shekel and a decrease of approximately 2.9% in relation to June 30, 2005.

The weakness of the dollar as compared with various currencies during the year 2006 has had a negative effect on the Group's profitability. See Section 3.4 to the Directors' Report.

To Section 6.5- interest rate fluctuations

During the quarter ended June 30, 2006, there was a rise of approximately 59% in the average rate of 3-month LIBOR interest, relative to the corresponding quarter last year and a rise of approximately 21% relative to the average LIBOR rate during the quarter ended on December 31, 2005. See Section 6.3 to the Directors' Report for further details.

2. Passenger Aircraft Area

To Sections 6.2-rise in traffic in the international aviation area, 7.1.3 (B) - developments in the Israeli market, 7.1.4-developments in markets of the operating area

Beginning from July 2006, Israel is carrying on warfare on two fronts: in the Gaza region and the Lebanese border, following the abduction of an IDF soldier by the Hamas faction and the abduction of two IDF soldiers by the Hezbollah group. During the hostilities, the IDF attacked targets in Lebanon and the Gaza Strip, while, on the other hand, the Hezbollah fired salvos of missiles at towns and cities in the North, threatening to extend the range of the strikes deep into Israel, and the Hamas faction continued to rain down Kassam rockets on towns and cities in the South. As a result, there were fatalities and severe property damage. It should be pointed out that a cease fire was declared on August 14, but as of the date of approval of this Report, IDF forces are still situated in Lebanon.

The hostilities have affected the Company's operations in a number of spheres, principally and most directly, a drastic decrease in the number of bookings and a significant rise in the quantity of cancellations, both by outgoing Israelis and by incoming tourists, and also higher security and operating costs. It should be stated that, based upon past experience, from the moment that the crisis ends, a relatively

[1] The update is being made 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 2005.

long period is required for recovery of incoming tourism traffic, and especially groups of tourists to Israel, this in comparison to the recovery of traffic of Israelis leaving the country which is anticipated to take less time. For example, it was only after approximately 6 years since the outbreak of the Intifada in the year 2000 that the level of incoming tourists to Israel approached the level that existed prior to the start of the Intifada. In addition, the hostilities may materially affect the Israeli economy, which, in itself, would have an indirect effect on the Company's operations and on its financial results. (See also the discussion on risk factors in the Periodic Report in Sections 9.18.1, 9.18.4, 9.18.7, 9.18.13.)

Due to the aforesaid, the Company estimates that the hostilities will have a material effect on the Company's financial results for the year 2006 (See the update to Section 9.16 below.)

To Sections 7.1.4-developments in markets, 7.1.10 - structure of competition in the operating area and changes that have taken place in it, 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, and in the update of the Sections itemized in the update of Chapter A in the financial statements as of March 31, 2006, it should be stated that, during the second quarter of the year 2006, there was an increase of approximately 29%, as compared with the same quarter last year, in the flight capacity of the scheduled foreign airlines to and from Israel (an increase due to additional frequency and/or the use of larger aircraft on the route). In total, there was growth in seat capacity at BGA (all companies, scheduled and charter) of approximately 13% in relation to the same quarter last year, while total traffic at BGA (scheduled and charter) rose by only approximately 9%.

The following are the outstanding examples of changes in operations of foreign airlines: Air France and Austrian airlines doubled the frequency of their flights from one daily flight to two daily flights (in total, 14 scheduled, weekly in place of 7 scheduled flights for each of the companies). Air Canada expanded the frequency of its weekly flights from 5 to 7, Iberia added 2 weekly flights and reached 12 flights weekly instead of 10, Turkish Airlines also increased the frequency of its weekly flights from 15 to 17. In addition, the Civil Aviation Authority approved the applications of British Airways and Lufthansa to expand the capacity of their seats without adding to flight frequency, by activating larger aircraft. Also, Israir, which, in May, began operating scheduled flights on the New York route increased the frequency of its weekly flights on the route in mid-June from 3 to 4 weekly flights.

The bulk of the growth in operations of the foreign airlines is evident in the Transatlantic routes, on which the capacity of the scheduled foreign companies increased by a total of approximately 60% versus the parallel quarter last year, and also in the routes to Western Europe on which the capacity of the scheduled foreign companies rose by a total of approximately 24% and the capacity of the foreign charter companies increased by approximately 40% compared to the same quarter last year.

It should be noted that, 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. (The Company claims that Air Madrid actually operated its flights as scheduled flights even though it was not authorized to do so.) In June 2006, Air Baltic also began to operate on the Tel-Aviv-Riga route.

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 for the year 2006 (see the update to Section 9.16 below).

To 7.1.5 Technological changes that could materially affect the operating sector

Section 7.1.5 made reference to the outfitting of the Company with broad band Internet technology for passengers during the flight (Project Connexion), including anticipated installations in the Company's aircraft. It should be noted that, at the beginning of July 2006, the Company received a notice from the Connexion Company of Boeing regarding the termination of marketing of the product due to problems at Boeing, and of their intention to consider various possibilities and methods of completing or selling the project. The Company is examining the implications of this notice on execution of the project by the Company.

In addition, it was stated that the Company is acting to execute significant expansion of its commercial capabilities via the Internet, including translation of its Internet site into additional languages, providing the resources to pay and sell abroad, etc.

To Section 7.4-new services

In addition to what was stated in Section 7.4 to the Periodic Report, it should be pointed out that, in July 2006, a direct flight route between Tel-Aviv and Los Angeles, U.S. was launched.

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

Continuing what was said in Section 7.11.1.B and in the update to this Section, as detailed in the update of Chapter A in the financial statements as of March 31, 2006, it should be stated that the period of leasing a 767-300 aircraft included in the table in the Section, which was to have terminated in March 2007, will be extended until February 2008.

3. Cargo Aircraft Area

To Section 6.1-rise in traffic in international aviation area and to Section 8.1.3 A - volume of world cargo transport

According to reports of IATA, during the months of January-May 2006, there was an increase of approximately 5.4% 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, the updated annual forecast of IATA for the year 2006 stands at 7%.

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 half of the year 2006, cargo activity at BGA increased by 1%, in comparison with the first half last year, this as opposed to the estimate of IATA which forecast annual growth at a volume of approximately 5%. At the same time, a rise of 5.4% was recorded in cargo activity at BGA during the second quarter of the year 2006, as compared with the second quarter last year.

To Section 8.1.5 - technological changes which could materially affect the operating area

In addition to what was itemized in Section 8.1.5 to the Periodic Report, it should be noted that the Company is acting to expand and develop advanced computerized solutions in the cargo area as well, with regard to the subject of internet commerce and the capability for self service, in order to better service and reduce costs to the Company.

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

In continuation to what was stated in Section 8.10, footnote 39, of the Periodic Report, and in the update of this Section as itemized in the update to Chapter A in the financial statements as of March 31, 2006, it should be stated that, during the month of July 2006, a contract was signed for the sale of the 747-200C aircraft, the operations of which were terminated in April 2006. (see Note 9 to the financial statements.)

Also, in continuation to what was stated in the update to Chapter A in the financial statements as of March 31, 2006 regarding negotiations for the possibility of selling an additional cargo aircraft and to the application of the Company in April 2006 to receive the approval of the holder of the Special State Share for the sale of the additional cargo aircraft, and for the reduction of the number of the Company's cargo aircraft to three, it should be noted that, through a date in proximity to the approval of this report, the authorization of the State had not yet been received.

4. Details Relating to the Two Operating Areas

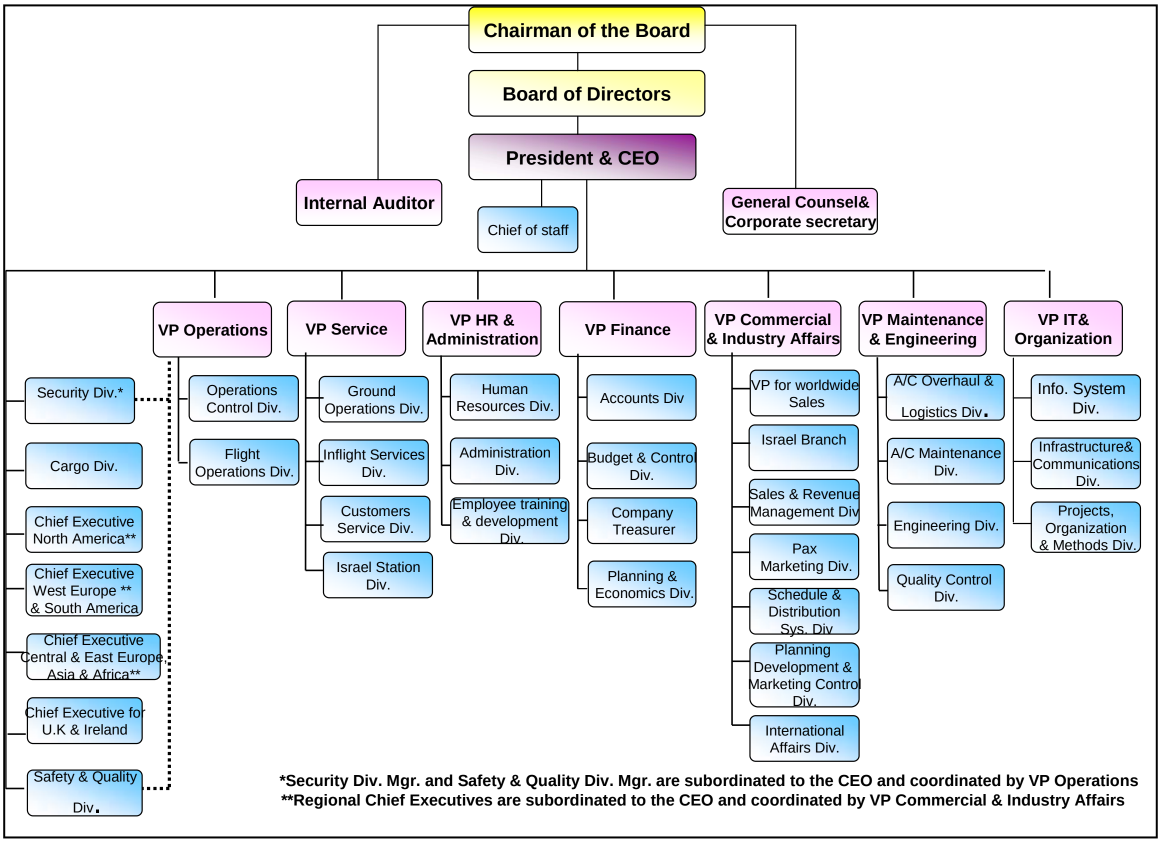
To Section 9.2- insurance

As the Company reported on July 3, 2006 in an Immediate Report on a Transaction or Commitment with a Controlling Shareholder which does not require the approval of a General Meeting, the Company responded to the request of Knafaim-Holdings Ltd. (hereafter: "Knafaim") and entered into an agreement with it according to which, on July 17, 2006, three insurance addendums were added to the Company's insurance policies in order to cover activities that are related to Knafaim: the "contingent stratum" addendum for 11 aircraft owned by the Knafaim Group, the "ground risks" addendum for 3 aircraft owned by the Knafaim Group and the addendum for third party liability related to maintenance activities provided by "Knafaim Maintenance" (an entity in the Knafaim Group) to aircraft of the air force. See the Immediate Report dated July 3, 2006 for the principal terms of this agreement between the Company and Knafaim.

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

In continuation to what was described in these Sections in the Periodic Report mentioned in the heading, and to the update of these Sections as itemized in the financial statements as of March 31, 2006:

1) As the Company reported in the Immediate Report dated July 3, 2006, a new VP for commerce and aviation relations, Mr. Avraham (Rami) Levi, was appointed and began to function as of August 1, 2006.
2) In July 2006, a new committee of the Board of Directors was established-the Committee for Business Development, for the purpose of promoting existing business of the Company and for the development of additional business.
3) In July 2006, an Employee Training and Development Division was established, under the auspices of the VP for human resources and administration. In addition, the function of chief of staff of the CEO, subordinate to the CEO, was set up.
   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 45. The number of members of the expanded management and other senior employees, mentioned in the table in Section 9.4.16 to the Periodic Report was updated to 35.
   The following is a diagram which describes the up-to-date organizational structure of the Company:



To Section 9.4.7-special collective agreements

In addition to what was stated in Section 9.4.7 of the Periodic Report, it should be noted that, in July 2006, a number of special collective agreements relating to air crew personnel and steward crew personnel were signed between the Company and the New General Workers Histadrut-the Division for Professional Unions and the employees' representatives for the purpose of improving the Company's operational flexibility by removing existing restrictions on carrying out direct flights without any stopover and shortening the stay of the crews in North America.

To Section 9.6.5 - working capital deficit

See updates in Section 2 to the Directors' Report.

To Sections 9.8.4, 9.8.5-loans for exclusive use

In July 2006, the Company signed a memorandum of intentions with a foreign bank to receive financing in an amount of approximately 80 million dollars against a lien on two 747-400 aircraft (with an option for an additional 10 million dollars for each aircraft to finance the cost of their modification to cargo-should it be decided to modify them for cargo). The Company has the right to withdraw the funds until the month of November 2007. The monies which will be received could be used for a prolongation of part of the existing loans or for other investments, as the Company elects at the time of withdrawing the loans. The financing is for a period of 10 years from the first withdrawal with quarterly payments of principal and interest.

To Section 9.11.7.2- designated carrier

In addition to what was stated in Section 9.11.7.2 of the Periodic Report, including and in particular in footnote 59, it should be noted that in conversations that were held recently between Israel and the Ukraine, it was agreed to change the current situation, in which a single designated carrier was determined, and carry out a changeover to an arrangement of designated carrier on the basis of "city pairs". Following this change, El Al filed a request with the Civil Aviation Authority to appoint it as designated carrier for all of the routes on which it had operated as a designated carrier prior to the change.

To Section 9.14-legal proceedings

1) In continuation to what was stated in Section 9.14.10 to the Periodic Report, in connection with a claim filed against the Company in July 2004 by the National Pilots Union, it should be noted that, in May 2006, a judgment was handed down to expunge the claim at the initiative of the Tribunal due to lack of action by the claimants.
2) In continuation to what was stated in Section 9.14.11 to the Periodic Report, in connection with a petition submitted by the Company to the Supreme Court to prevent a situation of inequitable arrangements and enforcement in the aviation sector by the Commissioner of Antitrust, it should be noted that on August 3, 2006, at per the Company's request, the Supreme Court ordered that the petition should be expunged while preserving the right to refile without having a claim of delay made against it.
3) In addition to what was stated in Section 9.14 to the Periodic Report, it should be noted that, in June 2006, a suit was filed against the Company and the State of Israel-Ministry of Finance in the Tel-Aviv District Labor Tribunal, by 94 claimants who were employed by the Company and took early retirement between the years 2001-2003. The claimants have appealed to amend their retirement agreements in a manner in which they state that the retiree will receive the early pension stipend, including fringe benefits, until the legal retirement age, instead of until the age of 65. Alternatively, the claimants appealed to revoke the retirement agreements. The Company is in the process of filing a defense writ.

To Section 9.16- forecasted developments in the coming year

1) As the Company reported in the Immediate Report dated July 19, 2006, as a follow up to reports and updates by the Company in the past in the context of the Periodic Report for the year 2005 and the reports for the first quarter of the year 2006, the trend of exacerbation in market conditions and the competitive business environment in which the Company operates, as well as the trend of rising prices of jet fuel, have continued. In view of this, and in light of recent developments in the security situation in Israel, the Company estimates that they will have a significant effect on its financial results for the year 2006, and that the year 2006 is expected to end in a loss, as to the extent of which the Company lacks materialized, forecasted data, this especially due to uncertainty on the security situation, its extent and its implications.
2) The Company's forecast of losses, as above in paragraph 1, is derived primarily from these factors:
   (A) The extreme worsening of market conditions and the competitive business environment in which the Company operates, due to the continuing effect of the trends and developments in this area of activity-see detail and information above in the update to Sections 7.1.4, 7.1.10, 7.8, 9.11.7.4 (developments in markets, competition and capacity).

(B) The ongoing trend of rising jet fuel prices-see Sections 6.3 and 9.5.1 to the Periodic Report, the update of those Sections in the update of Chapter A in the financial statements as of March 31, 2006 and the above update of those Sections. In the Company's estimation, based upon current jet fuel market conditions, the rise in jet fuel prices will add approximately 90 million dollars to the Company's operating expenses in comparison to the year 2005, after offsetting anticipated returns of hedging in both periods.

(C) The recent developments and the intensiveness of the security situation in Israel and their possible implications on the Israeli economy, in general, and on the Company's operations, in particular.-See details above in the updates to Sections 6.2, 7.1.3 (b), 7.1.4.

(D) Estimates and forecasts of the Company in connection with anticipated trends and developments in the industry during the third and fourth quarters of the year 2006.

3) The forecast included in this Section represents prospective information, as defined in the Securities Law, 1968. This data is information that is uncertain as it pertains to the future and is based principally on working assumptions, estimates and forecasts of the Company as they are known as of the date of this report, with relation to existing trends and anticipated developments in: the business environment in Israel and in the world, including the geopolitical and security situation and the rates of growth; the industry environment, including changes in passenger traffic (scheduled and charter) and cargo traffic, as well as changes in competition and the behavior and reactions of competitors; in external factors, including changes in jet fuel prices, interest rates, currency rates and security costs; in prices of supplies and expenses, including rates of commissions to agents, load factors on aircraft, retirement of personnel, Consumer Price Index in Israel and global supplies prices.

It should be emphasized that the actual results, in whole or in part, may not be realized as aforesaid, be realized only in part or differ substantially, positively or negatively, from the estimated results, which are derived or implied from this information, if the working assumptions, expectations and estimations of the Company are not realized. Realization of the above forecast in full or in part or in a manner which significantly varies from it (positively or negatively) or its non realization as aforesaid, could be affected, among other things, by the following principal factors:

(A) Additional significant changes in current competition in the areas of activity of the Company, for any reason and/or cause, and, in particular, under conditions where the Company will have difficulty reacting. Without detracting from the generality of this, changes in competition are likely to result, inter alia:

(1) From the entry of new competition into the market, additional flight capacity and/or flight frequency of companies that are presently operating, and from the business behavior of competitors, including in the area of prices;

(2) From regulatory changes and the manner of their application and/or changes in the aviation policies of the State of Israel and the manner of their implementation, including: civil aviation policies regarding the appointment of designated carriers in the network of routes and/or authorization of charter flights; civil aviation policies regarding the allowable capacity for foreign airlines (scheduled and charter);

(3) From expansion of the operations of "network" companies (which represent part of a global concordat) in the Israeli market in a manner which will make it difficult for the Company to join a concordat of this nature, and will impair its market share;

(4) From the entry into the market of the "low cost" companies and the degree of influence that this will have on the worsening of competition in the industry, the lowering of prices and the need to carry out a process of cost compatibility in the Company;

(5) From creation of a European aviation bloc which might fundamentally alter the structure of flight rights in the Market countries, to expand the number of companies and the sources of capacity between Israel and the Market countries on an unrestrained basis, and to impose a threat to the level of flight prices and the share of the Company in these routes;

(6) From imposition of limitations on the Company in the sphere of business restrictions.

(B) The Company currently bears exceptional expenses of security, which are out of its control, in relation to competing airlines. An increase or decrease in these expenses from the force of circumstances or due to a governmental decision, will definitely affect the Company's profitability;

(C) The possible implications of economic and/or security changes in the world, in general, and in Israel, in particular, on the volume of the Company's operations. These changes could impose a threat to the Company due to the lack of flexibility in its ability to carry out changes in part of the expense structure (such as flight equipment and salaries) and could create difficulties in implementing the process of conforming the Company's expenses;

(D) Fluctuations in jet fuel prices, which represents a substantial component of the Company's expenses, as well as the risks from varying currency and interest rates;

(E) Changes in the level of cooperation on the part of employees' associations with regard to updating labor agreements and observing "industrial tranquility".

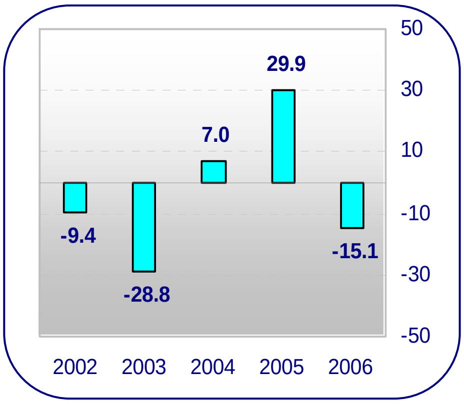
DIRECTORS' REPORT

EL AL ISRAEL AIRLINES LTD.

REPORT OF THE BOARD OF DIRECTORS CONCERNING THE COMPANY'S AFFAIRS FOR THE PERIOD ENDED JUNE 30, 2006

We are pleased to submit herewith the directors' report regarding the Company's state of affairs as of June 30, 2006.

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



During the second quarter the Company recorded a loss of $15.1 million ("m") as compared with a profit of $29.9m in the corresponding period last year.

The quarter's results were adversely affected by worsening market conditions, the competitive business environment along with rising jet-fuel prices and the revaluation of the shekel as well as the euro against the dollar.

Second-quarter revenues rose by 2% over the same period last year, totaling $429m.

Net cash provided by operating activities in the second quarter amounted to $50.3m, with the balances of cash and short-term investments on June 30, 2006 totaling $180.1m and shareholders' equity amounting to $245.5m.

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.

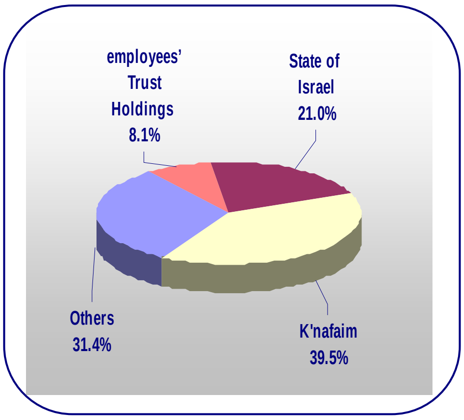
The Company's business environment constitutes international civil aviation to and from Israel, which is characterized by seasonal factors and fierce competition. This competition intensified during 2006 mainly due to the expanded activity of foreign airlines by the increased capacity, frequency of flights and use of larger planes that followed.

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 June 30, 2006:



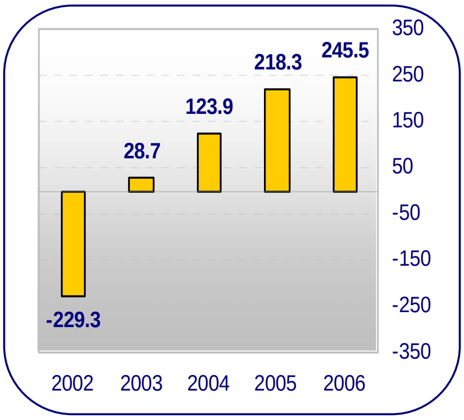
1.2 Privatization

On June 30, 2006 the shares in the Company were held by K'nafaim Holdings Ltd. ("K'nafaim") (39.5%), the state of Israel (21.0%), Holdings in Trust for the Employees of EL AL Ltd. (the employees' company) (8.1%) and others (31.4%).

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

2. Financial position (consolidated data)

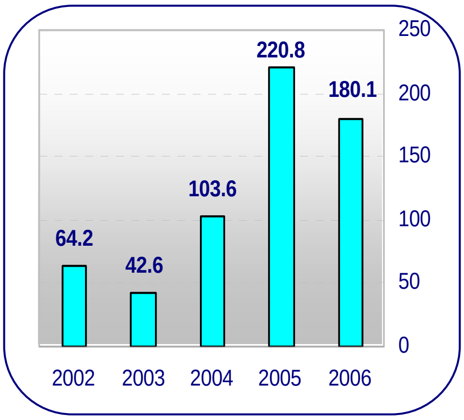
Shareholders' equity at June 30: (in millions US dollars)



	30.06.2006 in thousands US dollars	31.12.2005 in thousands US dollars	change in thousands US dollars	%
Assets				
Cash and short-term investments	180,101	206,763	(26,662)	(13%)
Trade accounts receivable	164,861	123,846	41,015	33%
Receivables	53,810	48,684	5,126	11%
Deferred income taxes	21,935	46,698	(24,763)	(53%)
Inventory	20,116	22,445	(2,329)	(10%)
Investments	5,719	5,846	(127)	(2%)
Fixed assets	1,164,551	1,163,765	786	0%
Other assets	3,322	4,671	(1,349)	(29%)
	1,614,415	**1,622,718**	**(8,303)**	**(1%)**
Equity & liabilities				
Short-term bank borrowings	63,788	75,713	(11,925)	(16%)
Trade accounts payable	147,185	155,046	(7,861)	(5%)
Payables and other current liabilities	407,849	324,546	83,303	26%
Long-term loans from financial institutions	608,034	627,363	(19,329)	(3%)
Accrued severance pay, net	119,438	120,526	(1,088)	(1%)
Deferred income taxes	21,507	46,300	(24,793)	(54%)
Other long-term liabilities	1,135	2,215	(1,080)	(49%)
Shareholders' equity	245,479	271,009	(25,530)	(9%)
	1,614,415	**1,622,718**	**(8,303)**	**(1%)**

Major changes in assets, liabilities and shareholders' equity on June 30, 2006 as compared with the balances of December 31, 2005:

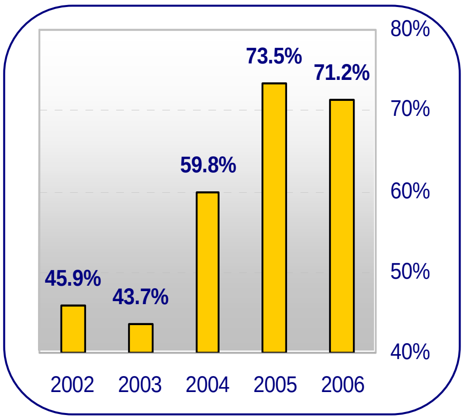
Cash and short-term investments at June 30: (in millions US dollars)



- A decrease in cash and short-term investments, stemming mainly from payments on account of aircraft purchases, investments in fixed assets and loan repayments which has partly been offset by cash flows provided by operating activities.
- An increase in trade accounts receivable, mainly due to higher passenger revenues.
- An increase in receivables and other current assets, stemming mainly from higher prepaid commissions due to an increase in passenger revenues.
- Decrease in short-term deferred-tax receivable along with a concurrent decline in the long-term deferred-tax liability stems from the classification of a tax asset (in respect of carry-forward losses) from short to long-term receivables in the first quarter of 2006.

- A decrease in inventory mainly due to jet-fuel consumption.
- The decrease in other assets is 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 Accounting Standard No. 22 of the Israeli accounting Standards Board.
- A decrease in trade accounts payable stemming, mainly from seasonal factors.
- A rise in payables and other current liabilities, mainly due to higher deferred income from sale of tickets not yet realized, as well as an increase accrued interest mainly due to the higher Libor rates.
- The balance of long-term loans (including current maturities) has declined mainly due to current repayments.
- A decrease in shareholders' equity stemming mainly from the loss for the period, net of the deposits made by the government to the severance-pay fund, which has raised the "capital reserve from transactions with a former controlling party", the exercises of options into shares and the reserve in respect of a benefit associated with the employee options program during the quarter.

Current ratio by % - at June 30:



On June 30, 2006 the Company had a working-capital deficiency of $178m and a current ratio of 71.2% as compared with $107m and 80.8% on December 31, 2005, respectively.

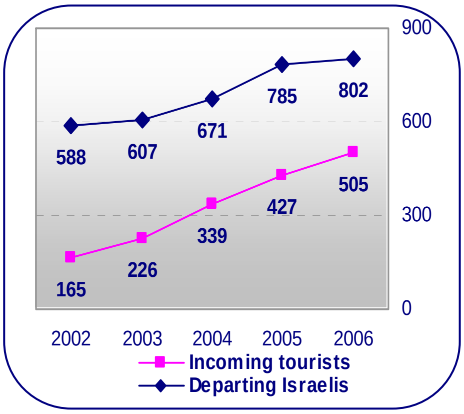
The increase in this deficiency stems mostly from declining cash, short-term investments and short-term deferred-tax receivable along with higher current liabilities arising from an increase in deferred revenues from the sale of flight tickets not yet realized.

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



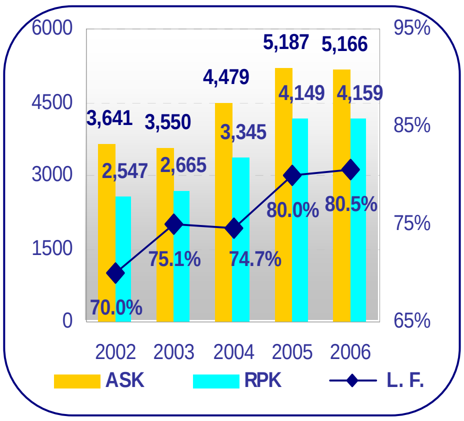
Passenger and cargo traffic at BGA	2006 in thousands	2005 in thousands	change in thousands	%
Apr - Jun				
Incoming tourists *	505	427	78	18%
Departing Israelis *	802	785	17	2%
Cargo import - tons **	33	31	2	5%
Cargo export - tons **	46	44	2	5%
Jan - Jun				
Incoming tourists *	891	752	139	18%
Departing Israelis *	1,363	1,289	74	6%
Cargo import - tons **	65	64	1	2%
Cargo export - tons **	97	97	1	1%

(*) Source: the Israeli Bureau of Statistics.

(**) Excluding cargo in transit.

3.2 Operating data

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



	Apr - Jun 2006	Apr - Jun 2005	change
Passenger leg (scheduled and chartered) - in thousands	919	921	(0%)
RPK (scheduled) - in millions	4,159	4,149	0%
ASK (scheduled) - in millions	5,166	5,187	(0%)
Load factor (scheduled)	80.5%	80.0%	1%
The Company's market share (scheduled and chartered)	39.6%	43.0%	(8%)
Cargo, in thousand tons	39	41	(5%)
RTK - in millions	207	225	(8%)
Weighted flying hours (including leased equipment) - in thousands (*)	44	44	0%
Average man-years (El AL only):			
Permanent	3,688	3,488	6%
Temporary	2,621	2,437	8%

	Jan - Jun 2006	Jan - Jun 2005	change
Passenger leg (scheduled and chartered) - in thousands	1,741	1,600	9%
RPK (scheduled) - in millions	7,953	7,335	8%
ASK (scheduled) - in millions	9,787	9,621	2%
Load factor (scheduled)	81.3%	76.2%	7%
The Company's market share (scheduled and chartered)	43.2%	44.5%	(3%)
Cargo, in thousand tons	85	85	0%
RTK - in millions	440	459	(4%)
Weighted flying hours (including leased equipment) - in thousands (*)	85	84	2%
Average man-years (El AL only):			
Permanent	3,674	3,474	6%
Temporary	2,530	2,255	12%
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	14.7	13.7	1.0

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.

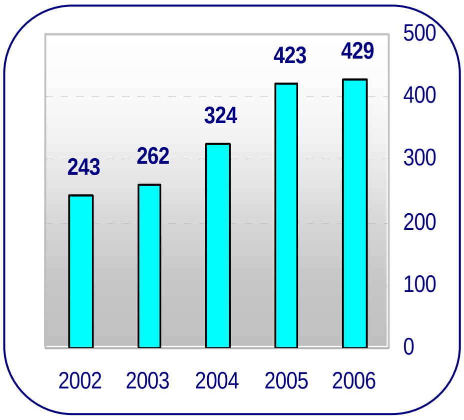
Passenger Load factor - Revenue Passenger Kilometer, expressed as percentage of Available Seat Kilometer.

*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.

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



3.3 Operating data:

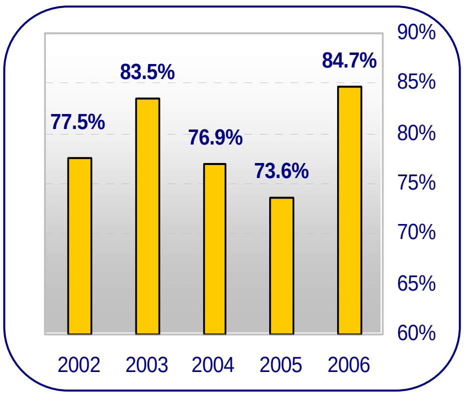
Three-month period ended June 30, 2006 (consolidated):

	Apr - Jun 2006 in thousands US dollars	Apr - Jun 2006 % of operating revenues	Apr - Jun 2005 in thousands US dollars	Apr - Jun 2005 % of operating revenues	change in thousands US dollars	change %
Operating revenues	429,200	100%	422,664	100%	6,536	2%
Operating expenses	(363,484)	(84.7%)	(311,214)	(73.6%)	(52,270)	17%
Gross profit	65,716	15.3%	111,450	26.4%	(45,734)	(41%)
Selling expenses	(47,896)	(11.2%)	(53,707)	(12.7%)	5,811	(11%)
General and administrative expenses	(23,121)	(5.4%)	(22,828)	(5.4%)	(293)	1%
Operating income (loss) before financing	(5,301)	(1.2%)	34,915	8.3%	(40,216)	
Financing expenses, net	(8,177)	(1.9%)	(4,405)	(1.0%)	(3,772)	86%
Other expenses, net	(1,591)	(0.4%)	(356)	(0.1%)	(1,235)	347%
Income taxes	(40)	(0.0%)	(227)	(0.1%)	187	(82%)
Income (loss) after taxes	(15,109)	(3.5%)	29,927	7.1%	(45,036)	
Company's equity in results of affiliates, net	53	0.0%	(61)	(0.0%)	114	
Net Income (loss) for the period	**(15,056)**	(3.5%)	**29,866**	7.1%	(44,922)	

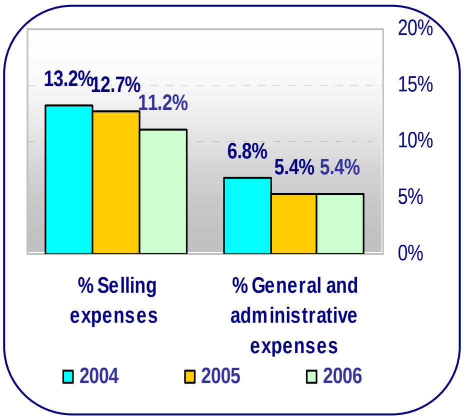
Major factors affecting the business results for the three-month period ended June 30, 2006 as compared with the corresponding period last year are as follows:

- The slightly higher operating revenues stemmed mainly from an increase in passenger income.
- Operating expenses rose in the second quarter of 2006 over the same period last year, mainly due to - higher jet-fuel prices and aircraft-leasing expenses, an increase in aircraft and flight-equipment maintenance expenses and a rise in wages, as detailed below.
- Average market jet-fuel prices rose during the second quarter of 2006 by 25% over the corresponding quarter last year, with the Company's jet-fuel expenses increasing by 18% from $98.4m to $116.6m, net of hedging rebates of $18.4m (same quarter last year - $16.0m). The rise in jet-fuel prices without a corresponding change in the volume of

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



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



activity added $21.3m to operating expenses (net of hedging rebates).

- Aircraft and flight-equipment maintenance expenses rose mainly from fluctuations in timing of engine repairs, higher cost of spare parts and the beginning of payments for additional engines whose insurance coverage had expired.

- Aircraft-leasing expenses rose mainly due to the addition of two 737-800 and one 767-300 aircraft.

- Selling expenses as well as their ratio to sales have declined from the same period last year.

- Current wages rose, among other reasons, due to an increase in the average workforce which stemmed from higher activity, a shekel revaluation in relation to the dollar in the quarter and an expense associated with the employee options program. As for the effect of the change in the shekel-dollar exchange rate on the Company's provisions - see item 3.4 below.

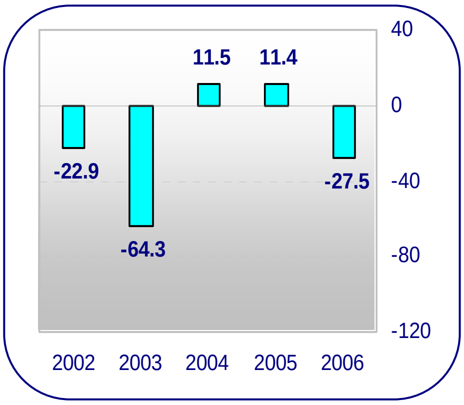
- Higher Libor interest rates and the shekel revaluation have led to an increase in financing expenses, offset by a reduction in total outstanding loans and by higher interest income on bank deposits (due to higher rates and currency hedging transactions).

Operating data:

Six-month period ended June 30, 2006 (consolidated):

	Jan - Jun 2006 in thousands US dollars	Jan - Jun 2006 % of operating revenues	Jan - Jun 2005 in thousands US dollars	Jan - Jun 2005 % of operating revenues	change in thousands US dollars	change %
Operating revenues	801,749	100%	742,087	100%	59,662	8%
Operating expenses	(678,317)	(84.6%)	(584,639)	(78.8%)	(93,678)	16%
Gross profit	123,432	15.4%	157,448	21.2%	(34,016)	(22%)
Selling expenses	(89,041)	(11.1%)	(94,798)	(12.8%)	5,757	(6%)
General and administrative expenses	(45,524)	(5.7%)	(43,435)	(5.9%)	(2,089)	5%
Operating income (loss) before financing	(11,133)	(1.4%)	19,215	2.6%	(30,348)	
Financing expenses, net	(15,135)	(1.9%)	(7,756)	(1.0%)	(7,379)	95%
Other expenses, net	(1,277)	(0.2%)	(5)	(0.0%)	(1,272)	25440%
Income taxes	(51)	(0.0%)	(256)	(0.0%)	205	(80%)
Income (loss) after taxes	(27,596)	(3.4%)	11,198	1.5%	(38,794)	
Company's equity in results of affiliates, net	95	0.0%	205	0.0%	(110)	(54%)
Net Income (loss) for the period	**(27,501)**	(3.4%)	**11,403**	1.5%	(38,904)	

Net income(loss) in the Jan - Jun by year: (in millions US dollars)



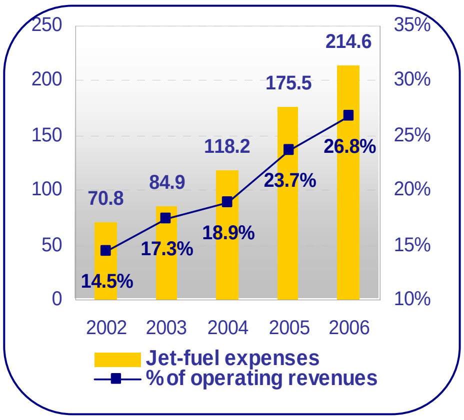
Major factors affecting the business results for the six - month period ended June 30, 2006 as compared with the corresponding period last year are as follows:

- The higher operating revenues stemmed mainly from an increase in the number of passengers flown, along with higher income from cargo due to an increase in the average income from ton/km flown.

- The Company's activity in the first half of 2006 rose over the same period last year, as reflected by passenger leg, passenger/ km and weighted hours flown. Operating expenses rose mainly due to higher volume and an increase in jet-fuel prices, higher aircraft leasing expenses, an increase in aircraft and flight equipment maintenance expenses as well as an increase in wages, as detailed below.

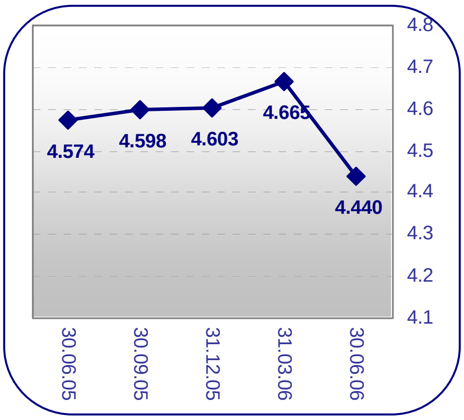
- Average market jet-fuel prices rose during the first half of 2006 by 26% over the corresponding period last year, with expenses increasing by 22% from $175.5m to $214.6m, net of hedging rebates of $34.5m (same period last year - $25.0m).

Total Jet-fuel expenses and % of operating revenues, Jan - Jun by years: (in millions US dollars)



- Aircraft and flight-equipment maintenance expenses rose mainly due to higher volume, fluctuations in timing of engine repairs, higher cost of spare parts and the beginning of payments for additional engines whose insurance coverage had expired.
- Aircraft-leasing expenses rose mainly due to the addition of two 737-800 and one 767-300 aircraft.
- Selling expenses as well as their ratio to revenues have declined from the same period last year.
- General and administrative expenses increased although, in relation to revenues, they have decreased from the same period last year.
- Current wages rose, among other reasons, due to an increase in the average workforce which stemmed from higher activity, a shekel revaluation in relation to the dollar in the quarter and an expense associated with the employee options program. As for the effect of the change in the shekel-dollar exchange rate on the Company's provisions - see item 3.4 below.
- Higher Libor interest rates and the shekel revaluation 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 currency hedging transactions).

Changes in US dollar exchange rate:



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 second quarter the shekel was revalued by 4.8% against the dollar, as compared with a devaluation of 4.9% in the same quarter last year.

During the first half of 2006 the shekel was revalued by 3.5% against the dollar, as compared with a devaluation of 6.2% in the corresponding period last year.

On June 30, 2006 the Company had liabilities totaling $160m in respect of severance pay, retirement programs, sick-leave and vacation pay. 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 second quarter there was an increase in expenses, due to this component, of $5.7m as compared with the reduction in expenses of $6.2m for the same period last year.

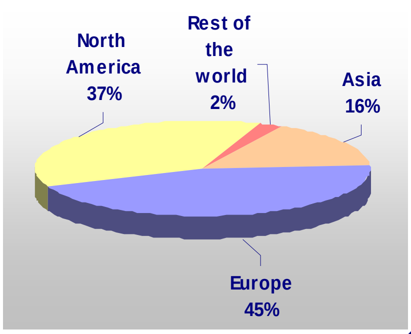
During the first half of 2006 there was an increase in expenses, due to this component, of $4.2m as compared with the reduction in expenses of $8.3m for the same period last year.

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

Three-month period ended June 30,	Before neutralizing the exchange-rate effect on the accrued severance pay 2006	Before 2005	After 2006	After 2005
	(in thousands US dollars)			
Operating expenses	363,484	311,214	359,931	314,671
Gross profit	65,716	111,450	69,269	107,993
Gross profit rate	*15.3%*	*26.4%*	*16.1%*	*25.6%*
Selling, general and administrative expenses	71,017	76,535	70,323	77,222
Operating income (loos) before financing expenses	(5,301)	34,915	(1,054)	30,771
Operating income (loos) rate before financing	(1.2%)	*8.3%*	(0.2%)	*7.3%*
Other expenses, net	1,591	356	138	2,373
Net income (loss) for the period	(15,056)	29,866	(9,356)	23,705
Net income (loss) for the period rate	(3.5%)	7.1%	(2.2%)	5.6%

Six-month period ended June 30,	Before neutralizing the exchange-rate effect on the accrued severance pay 2006	Before 2005	After 2006	After 2005
	(in thousands US dollars)			
Operating expenses	678,317	584,639	675,711	589,392
Gross profit	123,432	157,448	126,038	152,695
Gross profit rate	*15.4%*	*21.2%*	*15.7%*	*20.6%*
Selling, general and administrative expenses	134,565	138,233	134,056	139,195
Operating income (loos) before financing expenses	(11,133)	19,215	(8,018)	13,500
Operating income (loos) rate before financing	(1.4%)	*2.6%*	(1.0%)	*1.8%*
Other expenses, net	1,277	5	223	2,566
Net income (loss) for the period	(27,501)	11,403	(23,332)	3,127
Net income (loss) for the period rate	(3.4%)	1.5%	(2.9%)	0.4%

Operating revenues attributed to geographical segments – Apr - Jun 2006:



3.5 Reporting by segments

The following is a summary by geographical segments - consolidated:

Three-month period ended:				
30.06.2006 -(unaudited)	North America	Europe	Central Asia & Far East	Rest of the world
	(in millions US dollars)			
operating revenues	155.9	188.1	68.0	8.9
Operating income *	5.5	25.5	5.7	2.5
% of operating revenues	3.5%	13.6%	8.3%	28.2%
30.06.2005 -(unaudited)				
operating revenues	152.3	185.6	69.8	8.7
Operating income *	19.5	50.1	10.2	2.7
% of operating revenues	12.8%	27.0%	14.6%	30.7%

Six-month period ended:				
30.06.2006 -(unaudited)	North America	Europe	Central Asia & Far East	Rest of the world
	(in millions US dollars)			
operating revenues	278.8	348.4	143.2	17.7
Operating income *	4.3	44.8	23.7	4.9
% of operating revenues	1.5%	12.9%	16.5%	27.7%
30.06.2005 -(unaudited)				
operating revenues	257.6	322.7	132.3	16.2
Operating income *	21.6	69.7	15.3	5.2
% of operating revenues	8.4%	21.6%	11.6%	31.9%

Year ended:				
31.12.2005 -(audited)	North America	Europe	Central Asia & Far East	Rest of the world
	(in millions US dollars)			
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%

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

During the second quarter all segments enjoyed higher revenues over the same period in the previous year (except for Central Asia and the Far East) while operating income declined in all segments as compared with the same period last year. The lower operating income in the second quarter in all segments originated from passenger and cargo aircraft alike and stemmed from higher operating expenses, mainly the jet-fuel component (as explained in item 3.3 above).

Revenues from all geographical segments rose during the six-month period ended June 30, 2006 over the corresponding period last year.

Operating income for the first half of 2006 declined from the same period last year in all geographical segments, except for the Central Asia and Far East segment, which recovered from the aftermath of the T'sunami that had occurred in the first quarter of 2005.

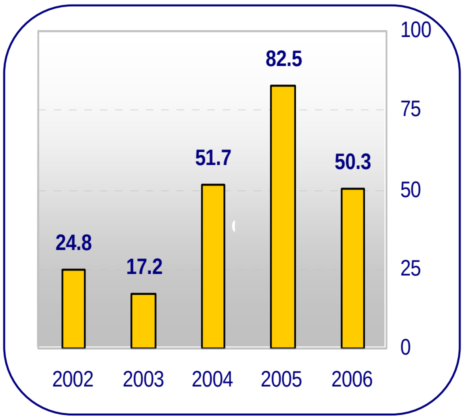
4. Seasonal factors

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

Cash flows from operating activities, second quarter by year:

(in millions US dollars)



	Apr - Jun 2006 in thousands US dollars	Apr - Jun 2005 in thousands US dollars	change in thousands US dollars
Cash flows from operating activities	50,319	82,546	(32,227)
Cash flows used for investing activities	654	(74,026)	74,680
Cash flows used for financing activities	(22,157)	(19,439)	(2,718)
Net increase (decrease) in cash	28,816	(10,919)	39,735

	Jan - Jun 2006 in thousands US dollars	Jan - Jun 2005 in thousands US dollars	change in thousands US dollars
Cash flows from operating activities	63,470	105,160	(41,690)
Cash flows used for investing activities	(26,144)	(85,984)	59,840
Cash flows used for financing activities	(30,154)	(24,888)	(5,266)
Net increase (decrease) in cash	7,172	(5,712)	12,884

The change in cash flows from operating activities in the second quarter of 2006 compared to the same period last year stemmed mainly from the loss for the period which was offset by net changes in assets and liabilities.

The change in the cash flows from operating activities in the first half of 2006 compared with the same period last year stemmed mainly from the loss for the period.

During the second quarter the Company used $21.2m 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 $22m in short-term deposits (as compared with the placement of new deposits amounting to a net $74.9m in the same period last year).

During the first half of 2006 the Company used $59.8m for payments on account of aircraft and fixed assets, spare parts and accessories (as compared with $23.2m in the corresponding period last year) while realizing a net $33.6m in short-term deposits (as compared with the placement of new deposits amounting to a net $75.2m in the same period last year). In total, the Company received $0.7m for its investment activities during the second quarter as compared with $74.0m used in the same quarter last year.

During the first half of 2006 the Company used $26.1m for its investment activities as compared with $86.0m.

During the second quarter the Company used $23.4m for repaying long-term loans (as compared with $22.5m for the same period last year).

During the first half of 2006 the Company used $29.5m for repaying long-term loans (as compared with $28.4m for the same period last year).

In total, the Company used during the second quarter $22.2m for financing activities, as compared with $19.4m in the same period last year.

In total, the Company used during the first half of 2006 $30.2m for financing activities, as compared with $24.9m in the same period last year.

Total cash and cash equivalents as well as short-term investments on June 30, 2006 amounted to $180.1m as compared with $206.8m on December 31, 2005 (June 30, 2005 - $220.8m).

During the second quarter the State deposited $0.3m to the employees’ severance-pay fund, in accordance with the terms of the prospectus.

During the first half of 2006 the State deposited $0.7m to the employees’ severance-pay fund, in accordance with the terms of the prospectus and the Company received $0.3m from the exercise of options (Series 1), also deposited to that fund.

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

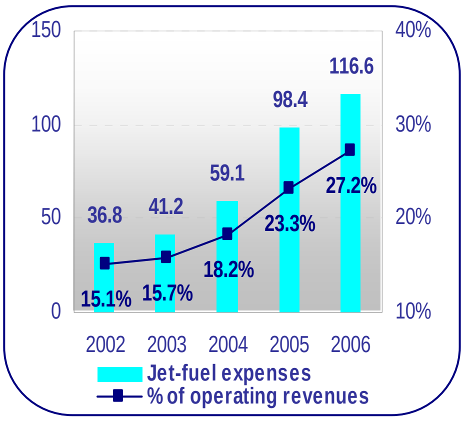
6.1 Company's policy for managing market risks, responsibility for managing them, means of supervision and policy implementation

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 exposures to existing risks while the CFO is responsible for carrying this policy out and reporting on it 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 for managing 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, second 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 June 30, 2006:

	Type of transaction	Period	Transaction's currency	Fair value in thousand US dollars
HJFP	Financial instruments	Up to One year	US dollar	31,567
HJFP	Financial instruments	Over One year	US dollar	5,278

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 its exposure to changes in interest rates on its long term credit loans. No additional transactions were carried out during the reported period.

Some of the abovementioned financial instruments, whose fair value on June 30, 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 June 30, 2006 were at fixed rates (for five years). According to the instruments chosen to protect the interest exposure, part of the above hedging transactions were effected at market rates, since the interest rate had passed the exit point established with the banks. at that time.

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 June 30, 2006 amounted to $1.4m and presented in the financial statements within “receivables and other current assets”.

7. Linkage

Consolidated linkage basis at June 30, 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	77,779	19,934	1,138	2,250	-	101,101
Short-term investments	79,000	-	-	-	-	79,000
Trade accounts receivable	148,718	257	7,521	8,365	-	164,861
Receivables and other current assets	15,482	4,554	1,895	1,480	30,399	53,810
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	63,585	-	-	-	1,100,966	1,164,551
Other assets	-	-	-	-	3,322	3,322
	385,793	**26,560**	**10,554**	**12,095**	**1,179,413**	**1,614,415**
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	(118,556)	(80,557)	(223)	(2,300)	(206,213)	(407,849)
Long-term loans	(608,034)	-	-	-	-	(608,034)
Accrued severance pay, net	(28,966)	(83,436)	(5,552)	(1,484)	-	(119,438)
Deferred income taxes	-	-	-	-	(21,507)	(21,507)
Other long-term liabilities	(1,135)	-	-	-	-	(1,135)
Shareholders' equity	-	-	-	-	(245,479)	(245,479)
	(915,582)	**(190,196)**	**(22,692)**	**(12,746)**	**(473,199)**	**(1,614,415)**
Monetary assets, net of monetary liabilities (monetary liabilities, net of monetary assets)	**(529,789)**	**(163,636)**	**(12,138)**	**(651)**	**706,214**	**-**

Consolidated linkage basis at June 30, 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	50,858	4,807	1,632	1,638	-	58,935
Short-term investments	161,857	-	-	-	-	161,857
Trade accounts receivable	156,159	259	6,738	13,740	-	176,896
Receivables and other current assets	12,851	3,798	2,457	1,849	25,154	46,109
Deferred income taxes	-	-	-	-	201	201
Inventory	-	-	-	-	11,788	11,788
Long-term bank deposits	-	1,691	-	-	-	1,691
Investment in another company	-	-	-	-	1,777	1,777
Investees	1,554	-	-	-	768	2,322
Fixed assets	7,504	-	-	-	1,151,598	1,159,102
Other assets	-	-	-	-	4,555	4,555
	390,783	**10,555**	**10,827**	**17,227**	**1,195,841**	**1,625,233**
Liabilities & Equity						
Short-term borrowings	(82,541)	-	(144)	(88)	-	(82,773)
Trade accounts payable	(99,014)	(27,199)	(16,037)	(11,452)	-	(153,702)
Payables and other current liabilities	(103,996)	(80,598)	(136)	(1,896)	(197,119)	(383,745)
Long-term loans	(653,040)	-	-	-	-	(653,040)
Accrued severance pay, net	(16,234)	(107,573)	(5,054)	(1,298)	-	(130,159)
Deferred income taxes	-	-	-	-	(216)	(216)
Other long-term liabilities	(3,312)	-	-	-	-	(3,312)
Shareholders' equity	-	-	-	-	(218,286)	(218,286)
	(958,137)	**(215,370)**	**(21,371)**	**(14,734)**	**(415,621)**	**(1,625,233)**
Monetary assets, net of monetary liabilities (monetary liabilities, net of monetary assets)	**(567,354)**	**(204,815)**	**(10,544)**	**2,493**	**780,220**	**-**

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, the independent auditors drew attention to Note 7 concerning the Company's exposure to lawsuits approved as class action. Although such a topic does not justify a qualification, this notation is required due to its potential material impact on the Company.

9. Subsequent events

As for events taking place subsequent to the balance-sheet date (sale of a cargo aircraft and an amendment to the CEO's employment contract) - see Note 9 to the interim financial statements.

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

August 16, 2006

Appendix to the Directors' report on the Company's business affairs for the six-month period ended June 30, 2006

Minimal disclosure required in valuations and rules pertaining to their inclusion with reports required by The Israeli Securities Regulations (Periodic and Immediate Financial Statements), 1970

Valuation of the 747-400 and 767 fleets

a. Overview

Accounting Standard No.15 ("Asset Impairment"), which was approved by the professional committee of the Israeli Accounting Standards Board, is based on International Accounting Standard No.36, which establishes rules for the required accounting treatment, presentation and disclosure in the event of impairment in the value of assets.

The standard's objective is to establish rules to be followed by a company in order to ensure that its assets are not presented in amounts exceeding their recoverable values. An asset that is presented in the balance sheet above its recoverable and realizable values indicates impairment and, accordingly, based on Standard No.15, the company must recognize a loss in respect thereof.

The following document presents the highlights of a valuation carried out by the Company's management in order to ascertain whether it is necessary to recognize any impairment in the value of its 747-400 and 767 fleets in accordance with Standard No. 15 and based on the guidelines of the Israeli Securities Authority.

This document has been prepared in accordance with The Israeli Securities Authority Regulations (Periodic and Immediate Financial Statements), 1970 ,concerning the minimal disclosure required in valuations and in respect thereof as well as to the rules pertaining to their inclusion in reporting pursuant to Securities Law, 1968

b. Details and Identification of the assets group

The group of assets for valuation consists of the following 10 planes:

Four 747-400 owned aircraft.

Six 767 owned aircraft.

c. Effective date

The valuation, which was performed in August 2006, was based on financial data for 2006 along with forecast for future years.

d. Appraiser

The valuation was carried out by the Company's management.

e. Circumstances giving rise to valuation according to standard 15

The fleet’s book value exceeds market value published by AVAC - the Aircraft Value Analysis Company and by Airclaims Company. It should be noted that the use of this market value is common and acceptable by many airlines around the globe as well as financing banks and EL AL in its various engagements.

As noted, Standard No.15 states that a company should write down the value of its assets whenever book value exceeds recoverable amount. The recoverable amount is the higher between the asset’s net selling prices or value in use.

Net selling price is the amount received from the sale of the asset in a transaction executed in good faith at arm’s length. The asset’s value in use equals the present value of future cash flows expected from the continued use of the asset and its realization at the end of the period of use. The Company considers the assets’ market value (as determined by AVAC) as representing net selling price. As of the date of this valuation, the Company has examined the value in use of its owned aircraft currently in use and whose net book value in the Company’s balance sheet on June 30, 2006 exceeds their selling price.

As of the date of this valuation the selling price of the 747-400 and 767 fleets (see item b above) amounts - on June 30, 2006.- to $259m and $58m, respectively as compared to a net book value of $284m and $64m, respectively

f. Valuation method

The valuation was performed by the cash-flow-capitalization method, according to which estimates of expected future cash flows from the use of the fleet were capitalized. The following major assumptions were used in the computations:

- Useful life - four years of activity (and aircraft realization at net selling prices after that period) for the 767 fleet and nine years for the 747-400 fleet (and aircraft realization at net selling prices after that period).
  It should be noted that for the 747-400 fleet the Company used in the past to apply the DCF computations over a four-year period yet now reached the conclusion, based on past experience and global practice, that the average useful life of these planes is estimated at 20 years so that this fleet's average useful life at EL AL is estimated at nine years.
- Expected cash flows from operating activities - management estimated that the cash flows from operating the above fleets during 2006 amounted to $49m and $47m for the 747-400 and 767 fleet, respectively. This computation was based on the above fleets' revenues, net of commissions and variable expenses attributed to these fleets and net of fixed cash outlays, such as security and maintenance which may be allocated in proportion to these fleets' operating cost. The computation of the cash flow at June 30, 2006 is lower than the one computed in previous years, mainly due to the higher jet-fuel prices.
- Disposal value at the end of the average useful life (four and nine years for the 767 and 747-400, respectively), which has been computed based on the AVAC and Airclaims forecasts, amounted to $38m and $86m for the 767 and 747-400 fleets, respectively (in no-capitalized values).
- Growth rates: due to conservatism, real future growth in the activities of these fleets has not been taken into account.
- Discount rate: assumed at 8%, which - in management’s opinion -adequately reflects the Company’s capital cost.
- Fleets' future Load Factor was set at a fixed rate, similar to 2006.
- Company’s effective tax rate during the next nine years - zero.
- No additional, unexpected investments have been assumed for the fleets in order to be able to continue use of these planes.

g. Value determined based on cash-flow capitalization

The following table presents a summary of the computation based on the DCF method:

747-400 fleet

	2007	2008	2009	2010	2011	2012	2013	2014	2015	Total
in millions $										
Total capitalized cash flows	47	43	40	37	34	32	30	27	26	316
Total capitalized disposal value (at the end of nine years)	-	-	-	-	-	-	-	-	43	43

Total fleets' value based on the cash-flow capitalization method - $359m

767 fleet

	2007	2008	2009	2010	Total
in millions $					
Total capitalized cash flows	45	41	38	36	160
Total capitalized disposal value (at the end of four years)	-	-	-	28	28

Total fleets' value based on the cash-flow capitalization method - $188m

Sensitivity analysis to the fleets' value for changes in the discount rate and cash contribution, which - in management's opinion - constitute key factor that may alter the realization - value forecasts.

747-400 fleet

Capitalization rate / annual contribution	6.0%	6.5%	7.0%	7.5%	8.0%	8.5%	9.0%	9.5%
(in thousand US dollars)								
30,000	260,856	254,738	248,841	243,155	237,670	232,379	227,272	222,343
40,000	330,884	323,428	316,235	309,292	302,590	296,117	289,864	283,823
48,673	391,619	383,003	374,686	366,653	**358,894**	351,397	344,151	337,145
50,000	400,912	392,119	383,629	375,430	367,509	359,855	352,457	345,303
55,000	435,925	426,464	417,326	408,499	399,969	391,724	383,753	376,043
60,000	470,939	460,809	451,023	441,568	432,429	423,593	415,049	406,783
65,000	505,953	495,154	484,720	474,637	464,889	455,462	446,345	437,524

Sensitivity analysis pertaining to jet-fuel price and asset utilization over nine years

Jet-fuel price (cent per Galon)	annual contribution	NPV	Net book value	The surplus of NPV over net book value
	in millions $			
168	58	423	284	138
177	54	391	284	106
187	49	**359**	284	74
196	48	352	284	68
205	47	346	284	61

767 fleet

Capitalization rate / annual contribution	6.0%	6.5%	7.0%	7.5%	8.0%	8.5%	9.0%	9.5%
				in thousands us dollars				
25,000	119,138	117,775	116,439	115,129	113,843	112,582	111,345	110,131
35,000	154,813	153,129	151,477	149,855	148,264	146,702	145,168	143,663
46,590	196,161	194,104	192,085	190,103	**188,157**	186,246	184,370	182,527
50,000	208,326	206,160	204,033	201,945	199,895	197,881	195,904	193,962
55,000	226,164	223,837	221,552	219,308	217,105	214,941	212,816	210,728
60,000	244,002	241,514	239,071	236,671	234,315	232,001	229,728	227,494
65,000	261,839	259,191	256,589	254,035	251,526	249,061	246,639	244,260

Sensitivity analysis pertaining to jet-fuel price and asset utilization over four years

Jet-fuel price (Cent per Galon)	annual contribution	NPV	Net book value	The surplus of NPV over net book value
	in millions $			
169	54	213	64	149
179	50	201	64	137
187	47	**188**	64	124
198	46	187	64	123
207	46	186	64	122

h. Summary

The following table presents a summary of the computation as of August 2006:

Computation of recoverable amount:

Fleet	Net selling price	Company's value in use	Company's recoverable amount - the higher of the two
in millions $			
747-400	259	359	359
767	58	188	188

Should a provision for impairment be recorded?

Fleet	Fleet's net book value - June 30, 2006	Fleet's recoverable amount to EL AL - August 2006	Should a provision for impairment be recorded?
in millions $			
747-400	284	359	NO
767	64	188	NO

This valuation is in effect at the time of its preparation and is based on an estimate of the 2006 financial data as well as income and expense estimates for the next four and nine years, respectively. Any change in the assumptions outlined above will change this valuation.

FINANCIAL STATEMENTS

EL AL ISRAEL AIRLINES LTD.
CONDENSED CONSOLIDATED
INTERIM FINANCIAL STATEMENTS
AS OF JUNE 30, 2006
(unaudited)

EL AL ISRAEL AIRLINES LTD.

Contents

Deloitte.

TRANSLATION OF THE HEBREW FINANCIAL STATEMENTS

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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 June 30, 2006 and for the six and three-month periods 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 June 30, 2006 and the condensed consolidated interim statements of operations, changes in shareholders' equity and cash flows for the six and three-month periods 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 condensed interim financial statements of subsidiaries whose assets constitute 0.5% of total assets included in the condensed interim consolidated balance sheet and whose revenues constitute about 0.3% of total revenues included in the condensed interim consolidated statements of operations for the six and three-month periods ended June 30, 2006.

Since the performed review is limited in scope and does not constitute an audit in accordance with generally accepted auditing standards, we do not express an opinion on the aforementioned condensed 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 financial statements for them to be deemed prepared in conformity with generally accepted accounting principles and in accordance with Chapter 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
Tel Aviv, August 16, 2006

Audit.Tax.Consulting.Financial Advisory.

Member of
Deloitte Touche Tohmatsu

EL AL ISRAEL AIRLINES LTD.
CONDENSED CONSOLIDATED INTERIM BALANCE SHEETS

	June 30,		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	101,101	58,935	93,929
Short-term investments	79,000	161,857	112,834
Trade accounts receivable	164,861	176,896	123,846
Receivables and other current assets	53,810	(*) 46,109	48,684
Deferred income taxes	21,935	(*) 201	46,698
Inventory	20,116	11,788	22,445
	440,823	455,786	448,436
Investments			
Long-term bank deposits	1,815	1,691	1,779
Investment in another company	1,945	1,777	1,878
Investees	1,959	2,322	2,189
	5,719	5,790	5,846
Fixed assets	1,164,551	1,159,102	1,163,765
Other assets	3,322	4,555	4,671
	1,614,415	1,625,233	1,622,718

(*) Reclassified.

EL AL ISRAEL AIRLINES LTD.
CONDENSED CONSOLIDATED INTERIM BALANCE SHEETS

	June 30, 2006	June 30, 2005	December 31, 2005
	(unaudited)	(unaudited)	(audited)
	(in thousand US dollars)		
Current liabilities			
Short-term borrowings and current maturities	63,788	(*) 82,773	75,713
Trade accounts payable	147,185	153,702	155,046
Payables and other current liabilities	407,849	(*) 383,745	324,546
	618,822	620,220	555,305
Long-term liabilities			
Long-term loans from financial institutions	608,034	653,040	627,363
Accrued severance pay, net	119,438	130,159	120,526
Deferred income taxes	21,507	(*) 216	46,300
Other long-term liabilities	1,135	(*) 3,312	2,215
	750,114	786,727	796,404
Total liabilities	1,368,936	1,406,947	1,351,709
Shareholders' equity			
Share capital	131,536	131,318	131,318
Share premium	904	826	826
Capital reserve from transactions with a former controlling party	299,821	299,119	299,119
Capital reserve from an employee options program	973	-	-
Accumulated deficit	(187,755)	(212,977)	(160,254)
	245,479	218,286	271,009
	1,614,415	1,625,233	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, August 16, 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

	Six-month period ended June 30		Three-month period ended June 30		Year ended December 31
	2006	2005	2006	2005	2005
	(unaudited)				(audited)
	(in thousand US dollars)				
Operating revenues	801,749	742,087	429,200	422,664	1,619,469
Operating expenses	678,317	584,639	363,484	311,214	1,243,198
Gross profit	123,432	157,448	65,716	111,450	376,271
Selling expenses	89,041	94,798	47,896	53,707	198,591
General and administrative expenses	45,524	43,435	23,121	22,828	88,758
	134,565	138,233	71,017	76,535	287,349
Operating income (loss) before net financing expenses	(11,133)	19,215	(5,301)	34,915	88,922
Net financing expenses	15,135	7,756	8,177	4,405	20,606
Operating income (loss) after net financing expenses	(26,268)	11,459	(13,478)	30,510	68,316
Other expenses, net	1,277	5	1,591	356	4,519
Pre-tax income (loss)	(27,545)	11,454	(15,069)	30,154	63,797
Income taxes	(51)	(256)	(40)	(227)	(304)
Income (loss) after income taxes	(27,596)	11,198	(15,109)	29,927	63,493
Company's equity in earnings (loss) of affiliates, net	95	205	53	(61)	633
Net income (loss) for the period	(27,501)	11,403	(15,056)	29,866	64,126
Basic earnings (loss) per share - in dollars	(0.07)	(*) 0.03	(0.04)	(*) 0.08	(*) 0.16
Number of shares used in the computation of basic EPS (in thousands)	400,570	399,483	400,773	399,563	399,633
Fully diluted earnings per share - in dollars	-	0.02	-	0.06	0.13
Number of shares used in the computation of fully diluted EPS (in thousands)	-	495,721	-	495,721	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	Share premium	Capital reserve (*)	Capital reserve (**)	Accumulated deficit	Total
	(in thousand US dollars)					
Six-month period ended June 30, 2006 (unaudited):						
Balance - January 1, 2006	131,318	826	299,119	-	(160,254)	271,009
Receipts on account of government of Israel debt	-	-	702	-	-	702
Exercise of options into shares	218	78	-	-	-	296
Benefit value of options program (see Note 6.3)	-	-	-	973	-	973
Loss for the period	-	-	-	-	(27,501)	(27,501)
Balance –June 30, 2006	131,536	904	299,821	973	(187,755)	245,479
Three-month period ended June 30, 2006 (unaudited):						
Balance – April 1, 2006	131,525	900	299,486	-	(172,699)	259,212
Receipts on account of government of Israel debt	-	-	335	-	-	335
Exercise of options into shares	11	4	-	-	-	15
Benefit value of options program (see Note 6.3)	-	-	-	973	-	973
Loss for the period	-	-	-	-	(15,056)	(15,056)
Balance - June 30, 2006	131,536	904	299,821	973	(187,755)	245,479
Six-month period ended June 30, 2005 (unaudited):						
Balance - January 1, 2005	130,940	699	273,328	2,232	(224,380)	182,819
Differences (***)	-	-	-	(104)	-	(104)
Realization of an investment in 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	-	-	-	-	11,403	11,403
Balance - June 30, 2005	131,318	826	299,119	-	(212,977)	218,286
Three-month period ended June 30, 2005 (unaudited):						
Balance - April 1, 2005	131,247	802	299,119	2,128	(242,843)	190,453
Realization of an investment in an investee	-	-	-	(2,128)	-	(2,128)
Exercise of options into shares	71	24	-	-	-	95
Net income for the period	-	-	-	-	29,866	29,866
Balance - June 30, 2005	131,318	826	299,119	-	(212,977)	218,286

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	Share premium	Capital reserve (*)	Capital reserve (**)	Accumulated deficit	Total
	(in thousand US dollars)					
Year ended December 31, 2005 (audited):						
Balance - January 1, 2005	130,940	699	273,328	2,232	(244,380)	182,819
Differences (***)	-	-	-	(104)	-	(104)
Realization of an investment in 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 year	-	-	-	-	64,126	64,126
Balance - December 31, 2005	131,318	826	299,119	-	(160,254)	271,009

(*) From transactions with the former controlling party.
(**) From an employee options program.
(***) 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

	Six-month period ended June 30 2006	Six-month period ended June 30 2005	Three-month period ended June 30 2006	Three-month period ended June 30 2005	Year ended December 31 2005
	(unaudited)				(audited)
	(in thousand US dollars)				
CASH FLOWS – OPERATING ACTIVITIES					
Net income (loss) for the period	(27,501)	11,403	(15,056)	29,866	64,126
Adjustments required to present net cash flows provided by operating activities (Appendix A)	90,971	** 93,757	65,375	** 52,680	119,493
Net cash provided by operating activities (*)	63,470	105,160	50,319	82,546	183,619
CASH FLOWS – INVESTING ACTIVITIES					
Proceeds from realization of investments in investees	-	12,800	-	12,800	13,656
Investment in other assets	(901)	(1,031)	(901)	(602)	(1,485)
Additions to fixed assets (including payments on account of aircraft purchases)	(59,774)	(23,210)	(21,168)	(11,624)	(82,822)
Proceeds from disposals of fixed assets	388	197	179	74	954
Decrease (increase) in short-term deposits, net	33,594	(75,211)	22,000	(74,905)	(26,428)
Investment in long-term deposits	(101)	(180)	(33)	(86)	(368)
Realization of long-term deposits	368	342	297	316	678
Investment in supplier deposits	(46)	-	(46)	-	(121)
Redemption of supplier deposits	1	2	1	-	130
Dividends received, net of investees' earnings, net	-	155	-	-	-
Decrease in investments and loans to investees, net	327	152	325	1	151
Net cash provided by (used for) investing activities, net	(26,144)	(85,984)	654	(74,026)	(95,655)
CASH FLOWS – FINANCING ACTIVITIES					
Proceeds from exercise of options into shares	296	505	15	95	505
Receipt of long-term loans from financial institutions	-	-	-	-	14,169
Repayment of long-term loans from financial institutions	(28,475)	(27,417)	(22,850)	(22,030)	(77,160)
Repayment of another long-term loan	(1,035)	(1,002)	(520)	(501)	(2,017)
Net increase (decrease) in short term bank borrowings	(940)	** 3,026	1,198	** 2,997	5,821
Net cash used for financing activities	(30,154)	(24,888)	(22,157)	(19,439)	(58,682)
Increase (decrease) in cash and cash equivalents	7,172	(5,712)	28,816	(10,919)	29,282
Cash and cash equivalents at the beginning of the period	93,929	64,647	72,285	69,854	64,647
Cash and cash equivalents at the end of the period	101,101	58,935	101,101	58,935	93,929
(*) Without depositing the issuance proceeds in the severance-pay fund for covering past liabilities.	63,755	**105,675	50,345	**82,622	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

	Six-month period ended June 30		Three-month period ended June 30		Year ended December 31
	2006	2005	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)	59,086	53,278	29,585	25,411	108,269
Adjustment in the value of long- term deposits	(63)	104	(90)	82	108
Equity in losses (earnings) of affiliates, net of dividends received (**)	(95)	-	(53)	61	(273)
Increase (decrease) in accrued severance pay, net	3,342	649	5,041	3,549	(10,298)
Increase in capital reserve from an employee options program	973	-	973	-	-
Capital gains from disposals of fixed assets, net	(118)	(130)	(51)	(36)	(590)
Capital gain from realization of investments in investees	-	(8,002)	-	(8,002)	(8,297)
Adjustment in value of supplier deposits	(22)	57	(23)	55	(51)
Deferred income taxes	(30)	-	(3)	-	(77)
Changes in assets and liabilities:					
Increase in trade accounts receivable	(41,015)	(65,716)	(5,411)	(32,274)	(12,667)
Decrease (increase) in receivables and other current assets	(5,125)	(13,193)	1,109	(11,568)	(16,087)
Decrease (increase) in inventory	2,329	(2,313)	(2,637)	(1,464)	(12,970)
Increase (decrease) in trade accounts payable	(7,861)	17,575	11,030	16,346	18,920
Increase in payables and other current assets	79,573	*111,451	25,900	*60,547	53,566
Increase (decrease) in other long-term liabilities	(3)	(3)	5	(27)	(60)
	90,971	93,757	65,375	52,680	119,493
(*) Reclassified.					
(**) Dividends received	-	360	-	-	360
Appendix B - Non-cash transactions					
Government deposits to the employees' severance-pay fund	702	25,791	335	-	25,791

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

EL AL ISRAEL AIRLINES LTD.
NOTES TO THE 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 Chapter D of 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, except for the notation made in item 1.3 below. 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/NIS and dollar/euro exchange rates:

	CPI (in points)	NIS/$	$/€
June 30, 2006	187.92	4.440	0.787
June 30, 2005	181.63	4.574	0.828
December 31, 2005	185.05	4.603	0.845
Change - %		%	
Six-month period ended			
June 30, 2006	1.6	(3.5)	(6.9)
June 30, 2005	0.5	6.2	13.0
Three-month period ended			
June 30, 2006	1.0	(4.8)	(4.5)
June 30, 2005	1.1	4.9	7.3
Year ended December 31, 2005	2.4	6.8	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 and for the six and three-month periods ended June 30, 2005 rose by $0.03, $0.01 and $0.02, respectively. The fully diluted EPS for 2005 and the six and three-month periods ended June 30, 2005 remained unchanged.

EL AL ISRAEL AIRLINES LTD.
NOTES TO THE FINANCIAL STATEMENTS

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

1.3 Initial implementation of new accounting standards (cont.)

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 program on which it was decided during the reported period starting the second quarter of 2006 - see Note 6.3.

EL AL ISRAEL AIRLINES LTD.
NOTES TO THE FINANCIAL STATEMENTS

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.

1.4 Effect of new accounting standards during the pre-implementation period

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

In July 2006 the Israeli Accounting Standards Board published Accounting Standard No.29 ("Adoption of International Financial Reporting Standards" - IFRS), which establishes that the financial statements of entities subject to the Israeli Securities Law and its reporting requirements, other than foreign corporations defined therein, will be prepared for reporting periods starting January 1, 2008 in accordance with the IFRS and their related clarifications published by the International Accounting Standards Board).An entity implementing the IFRS starting January 1, 2008 and electing to report comparative figures strictly for 2007 in accordance with the IFRS will be obliged to prepare an opening balance sheet at January 1, 2007 based on the IFRS. The transition to reporting according to the IFRS will be carried out in accordance with IFRS No.1 ("Initial Adoption of IFRS Standards"), which outlines rules for implementing the transition from financial reporting based on domestic accounting principles to reporting in accordance with the IFRS. IFRS No. 1 supercedes any transitional rules established in other IFRS (including those established in former domestic accounting standards), stating that all IFRS should be adopted retroactively for the opening balance sheet; nevertheless, IFRS No.1 grants allowances on certain issues by not applying the retroactive application in respect thereof. In addition, it contains certain exceptions in regard to the retroactive applications of certain aspects stipulated in other IFRS. Management is currently examining the effect of the transition to the IFRS standards yet is unable at this stage to assess its magnitude on the financial statements. The standard enables entities to chose between the preparation of their financial statements by the IFRS standards before January 1, 2008 for financial statements published subsequent to July 31, 2006. Management has not yet decided whether to adopt the IFRS standard early.

EL AL ISRAEL AIRLINES LTD.
NOTES TO THE FINANCIAL STATEMENTS

NOTE 2 - GENERAL

2.1 On July 19, 2006 the Company reported within the framework of immediate reporting that the market adverse conditions, along with high jet-fuel prices, had persisted. Consequently, and also in light of the security situation in Israel, the Company believes that these factors are likely to meaningfully affect its 2006 results, leading to a (not-yet-estimated) loss, especially in light of the uncertainty associated with the present security situation. These forecasts stem mainly from an additional meaningful deterioration in the market conditions and competitive business environment, along with the rising jet-fuel prices and worsening security situation in Israel, with its potential ramifications on the Israeli economy in general and the Company's activity in particular as well as the estimates and forecasts in regard to expected trends and developments in the aviation industry in the third and fourth quarter of 2006.

2.2 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 expands 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 six-month period ending June 30, 2006 the Company paid $38.3m to the Boeing Corporation on account of two ordered 777-200 aircraft plus $1.5m for an 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.

EL AL ISRAEL AIRLINES LTD.
NOTES TO THE FINANCIAL STATEMENTS

NOTE 5 - ACCRUED SEVERANCE PAY, NET

During the six-month period ending June 30, 2006 the Government of Israel deposited a total of $702 thousand to the severance-pay fund of the eligible employees, in respect of the proceeds it had received from the exercise of options. 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 six-month period ended June 30, 2006, the public exercised 1,003,247 options (Series 1) into an identical number of ordinary shares of NIS 1.00 par-value each, with the Company's proceeds - $296 thousand - deposited to the eligible employees' severance-pay fund.

6.2 On March 23, 2006 the General Meeting ratified an increase of NIS 54,279,453 in the Company's authorized share capital, bringing the 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 program ("Options Program 2006"). At the same time, the board approved that there would be a pool for allocation under this program, consisting of 17,092,129 options, exercisable into and up to 17,092,129 ordinary shares of NIS 1.00 par value each, subject to adjustments. The board will be authorized to increase the 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 by the audit committee on February 26, 2006, is subject to the ratification of the General Meeting for increasing the Company's authorized share capital. This ratification, along with the allotment, took place on March 23, 2006. 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 emanating 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 price (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).

EL AL ISRAEL AIRLINES LTD.
NOTES TO THE FINANCIAL STATEMENTS

NOTE 6 - SHARE CAPITAL AND SHARE PREMIUM

6.3 (Cont.)

According to the provisions of Accounting Standard No. 24 (“Stock-Based Payment”) of the Israeli Accounting Standards Board, the Company recorded option-granting expenses based on their economic value and computed by the Black & Scholes model. The expenses is recorded over the batch's "thawing" period, with the level of the expense constituting a function of the number of options granted as well as the economic value of each option.

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 28,287 thousand ($6.4m on the balance-sheet date) in respect of this program, reflecting - based on the Black & Scholes model - an average option price of NIS 1.75.

During the three-month period ended June 30, 2006 the Company recorded in respect of this program expenses totaling $973 thousand against a capital reserve. On May 23, 2006 the Company's board of directors decided to increase the number of the employee program's options by an additional 3m non-marketable options which may be exercised into and up to 3m ordinary shares of NIS 1.00 par value each.

The Company's board of directors appointed the Human Resources Appointment Committee to manage the 2006 options program, empowering it allot the abovementioned options to Company officers in accordance with parameters established by the board.

The options' theoretical exercise price will equal 85% of the average closing price on the Tel Aviv Stock Exchange of an ordinary share during the 30 days preceding the program manager's decision, except for recipients acting as vice president or division manager on March 23, 2006 and who had not received any options based on the allotment resolution of March 2006, in respect of which a theoretical price of NIS 2.9733 had been established.

EL AL ISRAEL AIRLINES LTD.
NOTES TO THE FINANCIAL STATEMENTS

NOTE 7 - CONTINGENT LIABILITIES

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

7.1 In October 1998, a lawsuit for NIS 230.4m ($52m 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.

7.2 A lawsuit for NIS 21.7m ($4.9m 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.

EL AL ISRAEL AIRLINES LTD.
NOTES TO THE FINANCIAL STATEMENTS

NOTE 8 - OPERATING SEGMENTS

Geographical segments - consolidated	North America	Europe	Central Asia & Far East	Rest of the world	Total
	(in thousand US dollars)				
Six-month period ended June 30, 2006 (unaudited)					
Revenues -					
Segment revenues	278,805	348,419	143,201	17,747	788,172
Revenues not allocated by segment					13,577
Total revenues (consolidated)					801,749
Operating income -					
Operating income, by segment	4,305	44,801	23,652	4,924	77,682
Net corporate expenses					(88,815)
Operating loss, before net financing expenses (consolidated)					(11,133)
Three-month period ended June 30, 2006 (unaudited)					
Revenues -					
Segment revenues	155,935	188,103	67,992	8,907	420,937
Revenues not allocated by segment					8,263
Total revenues (consolidated)					429,200
Operating income -					
Operating income by segment	5,532	25,516	5,650	2,532	39,230
Net corporate expenses					(44,531)
Operating loss, before net financing expenses (consolidated)					(5,301)

EL AL ISRAEL AIRLINES LTD.
NOTES TO THE FINANCIAL STATEMENTS

NOTE 8 - OPERATING SEGMENTS (Cont.)

Geographical segments - consolidated	North America	Europe	Central Asia & Far East	Rest of the world	Total
	(in thousand US dollars)				
Six-month period ended June 30, 2005 (unaudited)					
Revenues -					
Segment revenues	257,588	322,672	132,337	16,191	728,788
Revenues not allocated by segment					13,299
Total revenues (consolidated)					742,087
Operating income -					
Operating income by segment	21,575	69,713	15,341	5,158	111,787
Net corporate expenses					(92,572)
Operating income, before net financing expenses (consolidated)					19,215
Three-month period ended June 30, 2005 (unaudited)					
Revenues -	152,344	185,617	69,805	8,748	416,514
Segment revenues					6,150
Revenues not allocated by segment					422,664
Total revenues (consolidated)					
Operating income -					
Operating income by segment	19,542	50,135	10,170	2,690	82,537
Net corporate expenses					(47,622)
Operating income, before net financing expenses (consolidated)					34,915

EL AL ISRAEL AIRLINES LTD.
NOTES TO THE FINANCIAL STATEMENTS

NOTE 8 - OPERATING SEGMENTS (Cont.)

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 (consolidated)					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 net financing expenses (consolidated)					88,922

NOTE 9 - SUBSEQUENT EVENTS

9.1 In July 2006 the Company sold an owned cargo 747-200 aircraft, recording in its financial statements for the third quarter of 2006 a pre-tax capital gain of $6.2m.

9.2 On August 16, 2006 the audit committee and the board ratified an amendment to the CEO's employment contract, based on which the agreement's expiry date was established as December 31, 2010.