

GAZIT-GLOBE LTD.

Directors' Report to Shareholders **For the periods ended June 30, 2007**

The Board of Directors of Gazit-Globe Ltd. (hereinafter – “the Company”) is pleased to present the financial statements of the Company and its consolidated subsidiaries for the periods ended June 30, 2007:

1. A. General

The Company – directly and through its subsidiaries (hereinafter, collectively – “the Group”) and an affiliate – is engaged in the acquisition, development and management of income-producing properties in North America, Europe and Israel, focusing mainly on supermarket-anchored shopping centers. In addition, the Company is active in the senior housing communities and the medical office buildings sectors in North America. and continues to seek and realize opportunities within its core business and similar asset classes, both in regions where it operates and also in new territories.

B. Properties

As of the date of the financial statements, the Group owns 473 properties, as follows:

- 428 shopping centers and stores
- 22 shopping centers under development
- 12 senior housing communities (with approx. 1,231 units)
- 2 senior housing communities under development
- 7 medical office buildings and a multi-story parking garage
- 2 office buildings

The above properties have a gross leasable area (“G.L.A.”) of approximately 4.6 million square meters. They are recorded in the Company’s books and in the affiliate’s books at their fair value of NIS 42.1 billion and generate annual rental revenue of NIS 3.7 billion (annual rental revenue data is based on the gross annual rent from the properties currently owned at the exchange rate on the signing date of the financial statements).

In the U.S.A., the Company operates mainly through Equity One Inc. (hereinafter – “EQY”), a public company listed on the New York Stock Exchange (NYSE: EQY). EQY is a self-administrated, self-managed REIT (Real Estate Investment Trust) for U.S. tax purposes. As of the signing date of the financial statements, the Company owns, directly and indirectly (through the subsidiary, First Capital Realty Inc., as described below), 45% of EQY. EQY’s properties are located primarily in growing

metropolitan areas in the southeastern United States, mainly in Florida and Georgia, and in the Boston, Massachusetts metropolitan area. EQY owns 174 operating shopping centers, with a G.L.A. of 1.7 million square meters, as well as three land parcels for future development.

The Company is also active in the United States through Royal Senior Care (hereinafter – “RSC”) and ProMed Properties Inc. (hereinafter – “ProMed”). RSC, in which the Company holds a 50% interest, is active in the senior housing communities sector in the southeastern United States. RSC owns 12 senior housing communities, encompassing approximately 1,231 units, as well as two that are currently under development. ProMed, a wholly (100%) owned subsidiary, is engaged in the medical office buildings sector. ProMed owns seven medical office buildings in North America, with a G.L.A. of 68,000 square meters and a multi-story parking garage.

In Canada, the Company operates through First Capital Realty Inc. (“FCR”), a public company listed on the Toronto Stock Exchange (TSX: FCR). As at the signing date of the financial statements, the Company holds 53.8% of FCR. FCR’s properties are located primarily in growing metropolitan areas in the provinces of Ontario, Quebec, Alberta and British Columbia in Canada. FCR owns 157 properties in Canada, with a G.L.A. of approximately 1.8 million square meters and six shopping centers under development. In addition, FCR owns 14 million shares in EQY.

In Israel, the Company operates through Gazit-Globe Israel (Development) Ltd. (hereinafter – “Gazit Development”), which is 75% owned by the Company. Gazit Development is an owner, developer and operator of shopping centers in Israel and Bulgaria. It owns eight income-producing shopping centers in Israel, with a G.L.A. of approximately 107,000 square meters and has seven shopping centers under development. In addition, the Company owns an office building in Tel-Aviv, part of which serves as the Group’s headquarters.

In Europe, the Company operates mainly through Citycon Oyj. (hereinafter – “Citycon”), a Finnish public company, whose shares are listed on the Helsinki Stock Exchange (OMX). As of the signing date of the financial statements, the Company owns approximately 39.4% of Citycon’s share capital. Citycon is active in northern Europe (as of the signing date of the financial statements, in Finland, Sweden, Estonia and Latvia) and owns 84 shopping centers and retail properties. These properties are leased primarily to supermarkets and other retail chains, with a total G.L.A. of approximately 0.8 million square meters, and two shopping centers that are currently under development. The Company also operates in the European shopping centers sector (in Germany, as of the signing date of the financial statements) through wholly owned subsidiaries (hereinafter – “Gazit Europe”) and owns four shopping centers with a G.L.A. of approximately 40,000 square meters and two shopping centers under development. The Company is also active in Bulgaria, through wholly owned subsidiaries of Gazit Development (hereinafter – “Gazit Development (Bulgaria)”), where it owns a shopping center with a G.L.A. of approximately 7,000 square meters, two plots of land for the future development of shopping centers and offices, with an

area of approximately 153,000 square meters and also an office building that is used by the Group.

Other publicly accessible data concerning the Group, including up-to-date presentations, supplemental packages with information regarding assets, liabilities and other information (it is hereby clarified that such information does not constitute part of this report and is also not included as an invitation), can be found on the Group's Internet website and the Internet websites of the Group's companies:

www.gazit-globe.com
www.equityone.net
www.firstcapitalrealty.ca
www.citycon.fi

C. Highlights – Second quarter of 2007:

- **The Group and the affiliate's investments totaled NIS 1.5 billion, compared to NIS 1.1 billion in the corresponding quarter last year.**
- **Property rental revenue totaled NIS 683 million, an increase of 9% compared to the corresponding quarter last year. The increase is due to the enlargement of the property portfolio as a result of the acquisition of new properties, net of properties sold, the development properties coming on-line and the increase in the average rent per square meter received on the Group's properties.**
- **NOI⁽¹⁾ totaled NIS 465 million, compared to NIS 412 million in the corresponding quarter last year, an increase of 13%.**
- **FFO⁽²⁾ totaled NIS 65.2 million, NIS 0.55 per share, compared to NIS 61.7 million, NIS 0.58 per share, for the corresponding quarter last year, an increase of 6%.**

The decrease in FFO per share, in the amount of NIS 0.03, as referred to above, is due to the following reasons:

- 1. The appreciation in the average exchange rates between the aforementioned periods (the U.S. dollar – 9.5%, the Canadian dollar – 7%, and the euro – 2.8%), which has a NIS 4 million effect (NIS 0.03 per share).**

⁽¹⁾ NOI – Property rental revenue, net of property operating expenses.

⁽²⁾ See section 3D below.

2. A NIS 6.1 million (NIS 0.05 per share) increase in non-recurring administrative expenses), mainly due to transactions that did not ultimately take place.

- The principal operating items, according to the average exchange rates for the second quarter of 2006, are as follows:

	For the three months ended June 30		Rate of change between the periods
	2007	2006	
	NIS in millions		
Property rental revenue	<u>741</u>	<u>626</u>	<u>18%</u>
NOI	<u>504</u>	<u>412</u>	<u>22%</u>
FFO	<u>69</u>	<u>62</u>	<u>12%</u>
FFO per share	<u>0.58</u>	<u>0.58</u>	=

- Gross profit totaled NIS 462 million, compared to NIS 299 million in the corresponding quarter last year, an increase of 55%, which is mainly due to the first-time implementation of Israel Accounting Standard No. 16, see section H. below.
- Cash inflows from operating activities totaled NIS 234 million, compared to NIS 183 million for the corresponding quarter last year, an increase of 28%.
- Net income totaled NIS 368 million, NIS 3.06 per share, compared to NIS 126.5 million, NIS 1.16 per share, for the corresponding quarter last year.
- At the end of the quarter, the Group had 22 properties under development with a gross area of approximately 260,000 square meters, 22 properties being redeveloped and additional land reserves, costing approximately NIS 1.6 billion, which have been earmarked for future development. The additional cost to complete these properties under development and redevelopment totals NIS 2 billion.
- Capital reserves⁽¹⁾ (included within the line item “shareholders’ equity”) rose by NIS 368.1 million (NIS 3.1 per share), compared to a fall of NIS 43.7 million (NIS 0.41 per share) in the corresponding quarter last year. The increase in the capital surpluses is due to the strengthening of the Canadian dollar, the U.S. dollar and the euro against the shekel (a “devaluation” of the shekel) at the end of the quarter, compared to the weakening of the Canadian dollar, the U.S. dollar and the euro against the shekel (an “appreciation” of the shekel) in the corresponding quarter last year.

⁽¹⁾ Capital reserves deriving from translation of the financial statements of foreign operations.

- As of June 30, 2007, debt to market capitalization (derived from the market value of the Group's holdings) was 52.4%, the same as of June 30, 2006, compared 49.4% as of December 31, 2006.
- The Company is applying Israel Accounting Standard No. 16, "Investment Property", for the first time commencing from January 1, 2007. As a result of implementing the standard as stated, the Company's shareholders' equity as of December 31, 2006 increased from approximately NIS 2.9 billion to approximately NIS 4.6 billion. Moreover, in the second quarter of 2007, the Company recognized income from adjustments to the fair value of properties, according to its proportionate share, in the gross amount of approximately NIS 86 million (approximately NIS 71 million after providing for taxes).

D. Highlights – First six months of 2007 (hereinafter – “the reporting period”):

- The Group and the affiliate's investments totaled NIS 3.5 billion, a similar amount as in the corresponding period last year.
- Property rental revenue totaled NIS 1.3 billion, an increase of 3% compared to the corresponding period last year. The increase is due to the enlargement of the property portfolio as a result of the acquisition of new properties, net of properties sold, the development properties coming on-line and the increase in the average rent per square meter received on the Group's properties.
- NOI totaled NIS 893 million, compared to NIS 847 million in the corresponding period last year, an increase of 5%.
- FFO⁽¹⁾ totaled NIS 130.3 million, NIS 1.10 per share, compared to NIS 133.6 million, NIS 1.29 per share, for the corresponding period last year.

The decrease in FFO (NIS 3.3 million) and FFO per share (NIS 0.19) as referred to above, is due to the following reasons:

1. The appreciation in the exchange rates between the aforementioned periods (the U.S. dollar – 9.6%, the Canadian dollar – 9.1%, and the euro – 2.2%), which has a NIS 10 million effect (NIS 0.09 per share).
2. Expenses relating to The Mills Corporation (“MLS”) shares, which were sold at the end of the first quarter, in the amount of NIS 10 million (NIS 0.09 per share).
3. A NIS 6.1 million (NIS 0.05 per share) increase in non-recurring administrative expenses, mainly due to transactions that did not ultimately take place.
4. Sale of the Texas property portfolio in April 2006.

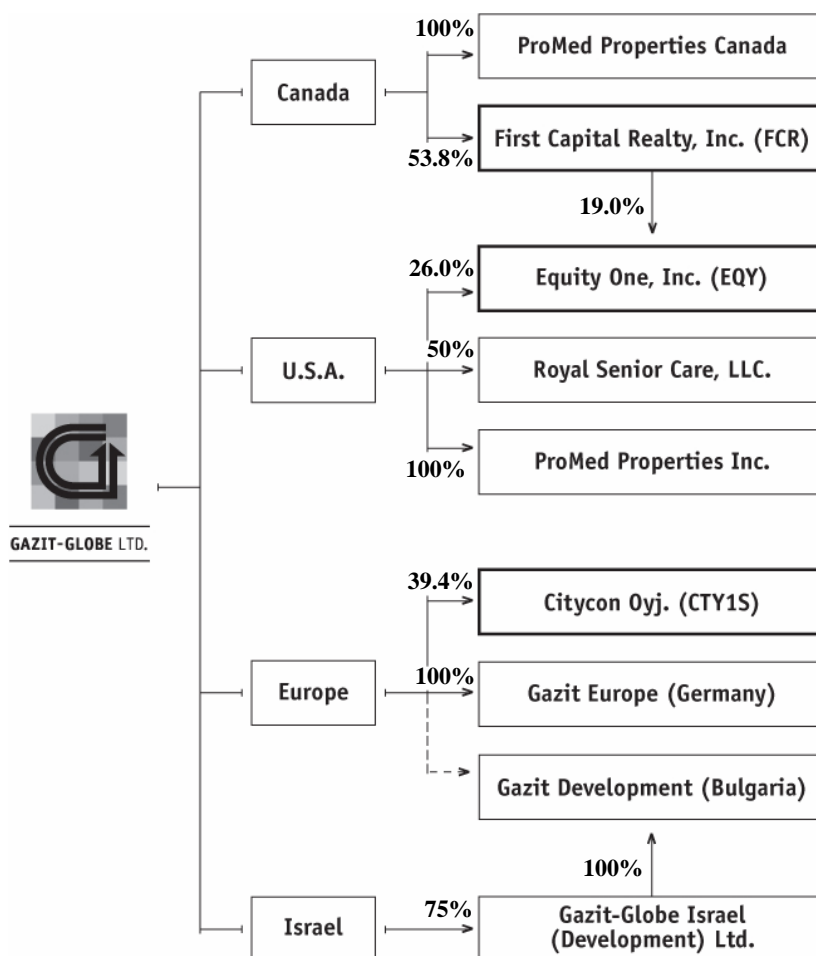
⁽¹⁾ See section 3D below.

- The principal operating items, according to the average exchange rates for the first six months of 2006, are as follows:

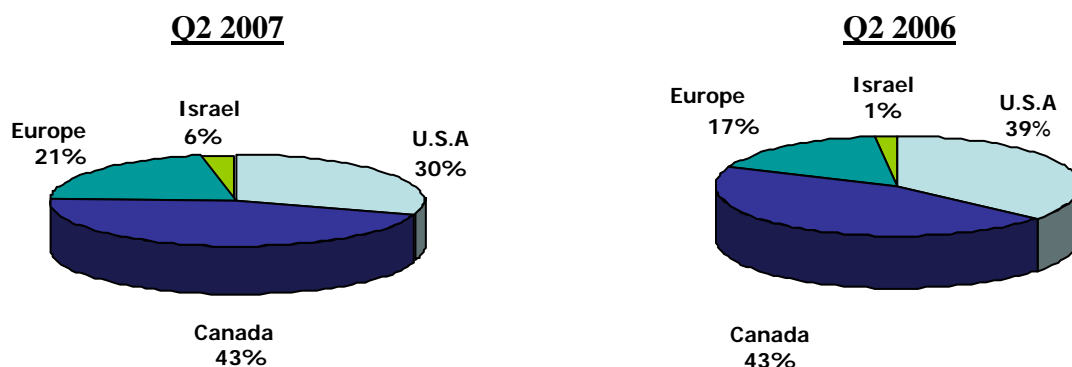
	For the three months ended June 30		Rate of change between the periods
	2007	2006	
	NIS in millions		
Property rental revenue	<u>1,457</u>	<u>1,287</u>	<u>13%</u>
NOI	<u>981</u>	<u>847</u>	<u>16%</u>
FFO	<u>141</u>	<u>134</u>	<u>5%</u>
FFO per share	<u>1.19</u>	<u>1.29</u>	<u>(8%)</u>

- Gross profit totaled NIS 888 million, compared to NIS 621 million in the corresponding period last year, an increase of 43%, which is due to the first-time implementation of Israel Accounting Standard No. 16, see section H. below.
- Cash inflows from operating activities totaled NIS 404 million, compared to NIS 338 million for the corresponding period last year, an increase of 20%.
- Net income totaled NIS 603.2 million, NIS 5.02 per share, compared to NIS 166.8 million, NIS 1.60 per share, for the corresponding period last year.
- The Company is applying Israel Accounting Standard No. 16, "Investment Property", for the first time commencing from January 1, 2007. As a result of implementing the standard as stated, the Company recognized, in the reporting period, income from adjustments to the fair value of properties, according to its proportionate share, in the gross amount of approximately NIS 276 million (approximately NIS 228 million after providing for taxes).

E. The Company's Major Holdings are Shown Below (Ownership Percentages are as of the Date of the Financial Statements):



F. Breakdown of Net Operating Income (“NOI”)⁽¹⁾, According to the Company’s Operating Regions:



⁽¹⁾ The Company's share (“by proportionate consolidation”), including its equity in an affiliate - see section G.2 below.

G. The Company's Assets:

1. The following table presents a summary of the Company's assets as of June 30, 2007, as shown above:

Name of company	Type of security/ property	Holding (millions)	Holding percentage (%)	Book value (NIS in millions) (¹)	Market value as of June 30, 2007 (NIS in millions)
EQY ⁽²⁾	Shares (NYSE)	17.1	23.2	1,471	1,854
FCR	Shares (TSX)	41.4	53.4	3,835	4,210
FCR	Convertible debentures (TSX)	105.3	42.1	436	440
Citycon	Shares (OMX)	76.0	39.5	1,924	2,006
Citycon	Convertible debentures (OMX)	37	33.6	215	271
RSC	Income-producing property	-	-	268	-
Property in Europe	Income-producing property	-	-	670	-
ProMed	Income-producing property	-	-	1,051	-
Property in Israel	Income-producing property	-	-	1,364	-
Total				11,234	-

⁽¹⁾ According to the fair value of the assets in conformance with Israel Accounting Standard No. 16 and at depreciated cost in conformance with Israel Accounting Standard No. 27.

⁽²⁾ Represents only the Company's direct interest in EQY. (In addition, FCR owns 14 million shares of EQY).

Below are the Company's monetary balances (including balances of subsidiaries that are not public companies) as of June 30, 2007 (NIS in millions):

Debentures and debts to financial institutions *	6,243
Monetary liabilities, other than debentures and debts to financial institutions	<u>347</u>
Total monetary liabilities	6,590
Less – monetary assets	<u>866</u>
Monetary liabilities, net	<u>5,724</u>

* Below are the annual repayments of the debentures and debts to other financial institutions (NIS in millions):

<u>Year</u>	<u>Total</u>	<u>%</u>
2007	74	1
2008	102	2
2009	160	3
2010	341	6
2011	491	8
2012	465	8
2013	448	7
2014	893	14
2015	485	8
2016	465	7
2017	209	3
2018	446	7
2019	461	7
2020	463	7
2021	614	10
2022 and after	<u>126</u>	<u>2</u>
Total	<u>6,243</u>	<u>100</u>

2. Additional information is presented below concerning the Company's share in the income-producing properties owned by the Group as of June 30, 2007, based on capitalized net operating income ("NOI")⁽¹⁾ methodology. The presentation of this information is intended to provide additional information, based on methodology that is generally accepted in the regions in which the Company operates, which might serve as an additional method in analyzing the value of the Company's properties on the basis of the Company's financial results for the reporting period. It is emphasized that this information does not represent the Company's present or future value of its assets.

The sensitivity analyses shown in the table below describe the implied value of the income-producing properties⁽²⁾ owned by the Group according to the range of different cap rates generally accepted in the regions in which the Group operates, as of the date of publishing the financial statements. It should be noted that this presentation does not take into account additional building rights that exist in respect of the Group's income-producing properties.

In calculating the NOI, the following assumptions were made:

- The NOI for the period for each of the Group companies.
- The Company's proportionate share in the NOI of the Group companies:

	For the three months ended June 30		For the year ended December 31,	
	2007	2006	2006	
N I S i n m i l l i o n s				
Property rental revenue	683	626	2,552	
Property operating expenses	(218)	(214)	(868)	
NOI for the period	465	412	1,684	
Less – minority's share in NOI	(239)	(221)	(893)	
Add – Company's share in Citycon's NOI	56	41	180	
NOI for the period	282	232	971	
NOI for the year	⁽³⁾1,129	⁽³⁾929	971	
Cap Rate:	<u>5.75%</u>	<u>6.00%</u>	<u>6.25%</u>	<u>6.50%</u>
Value of proportionately consolidated income-producing property (NIS in millions) ⁽⁴⁾	<u>19,631</u>	<u>18,813</u>	<u>18,060</u>	<u>17,366</u>

⁽¹⁾ NOI - Property rental revenue, net of property operating expenses.

⁽²⁾ NOI divided by the cap rate.

⁽³⁾ NOI for the second quarter of 2007 multiplied by 4.

⁽⁴⁾ In accordance with the NOI for the second quarter of 2007.

New properties and properties under development, which have not yet come on line and which are presented at their carrying values in the Company's books (according to the proportionate consolidation method) as of June 30, 2007, amounted to NIS 1,110 million.

The Group's liabilities, net of monetary assets (by the proportionate consolidation method) as of June 30, 2007, amounted to NIS 12,352 million.

3. **Net Asset Value (EPRA NAV and EPRA NNAV)**

As is customary in the European countries in which the Group is active, and in line with the position paper of the European Public Real Estate Association ("EPRA"), the objective of which is to promote greater transparency, uniformity and comparability of the financial information reported by property companies, the Company publishes net asset value data (EPRA NAV), which is an index that reflects the net asset value of the Company, with certain adjustments, e.g., the neutralization of the fair value revaluation adjustments in respect of derivative financial instruments, which are treated as hedging instruments from an economic perspective, but which do not meet the criteria for hedge accounting, and deferred taxes in respect of the revaluation of assets to their fair value; the Company also publishes EPRA NNAV data, which is another index reflecting net asset value (EPRA NAV), adjusted for the fair value of financial instruments of the kind referred to above and for the fair value of financial liabilities, and also with certain adjustments to the provision for deferred taxes.

The Company considers that presentation of EPRA NAV and EPRA NNAV data enables the Company's results to be compared with those of other European property companies. At the same time, these data do not constitute a valuation of the Company and do not replace the other data presented in the financial statements; rather, they provide an additional aspect to assist investors in understanding the Company's results in accordance with the recommendations of EPRA.

Presented below is the calculation⁽¹⁾ of the EPRA NAV and EPRA NNNAV:

	As of June 30, 2007 NIS in thousands
a. <u>EPRA NAV</u>	
Shareholders' equity per financial statements	5,509,768
Adjustments for neutralization of fair value of financial instruments	79,153
Add – Provision for tax on revaluation of investment property to fair value (net of minority's share)	<u>968,659</u>
Net asset value - EPRA NAV	<u>6,557,580</u>
EPRA NAV per share (in NIS)	<u>55.6</u>
b. <u>EPRA NNNAV</u>	
EPRA NAV	6,557,580
Adjustment for addition of fair value of financial instruments	(19,007)
Adjustments of financial liabilities to fair value	(194,762)
Other adjustments to provision for deferred taxes	<u>-</u>
“Adjusted” net asset value - EPRA NNNAV	<u>6,343,811</u>
EPRA NNNAV per share (in NIS)	<u>53.8</u>

4. As of June 30, 2007, the Company's issued share capital comprises 118 million shares (excluding treasury stock held by the Company).

⁽¹⁾ Comparative data are not relevant for this index, since - in the financial statements - the comparative data for the investment property is not presented on the basis of fair value.

H. Change in Shareholders' Equity and Reported Income Due to Changes in Accounting Standards:

With effect from January 1, 2007, the Company applies Israel Accounting Standard No. 16, "Investment Property" (hereinafter – "the Standard"), of the Israel Accounting Standards Board. The Standard prescribes the accounting treatment and disclosure requirements with regard to investment property.

Investment property is defined as property (land or a building – or part of a building – or both) held (by the owner or by the lessee under a finance lease) to earn rentals or for capital appreciation (or both) and which is not held for use in the production or supply of goods or services or for administrative purposes or for sale in the ordinary course of business.

The main changes prescribed by the Standard as compared to the accounting principles that were applied prior to January 1, 2007, are:

Investment property is to be presented according to the cost model or at fair value. The Company has opted to apply the fair value model as its accounting policy for the presentation of investment property. The Company has reported the effect of adopting the Standard from January 1, 2007 as an adjustment to the opening balance of the retained earnings at that date.

Property rights held by a lessee under an operating lease from the Israel Lands Administration are classified as investment property. The Company will apply the fair value model in respect thereto.

Presented below are details of the effect of the Standard, which has been carried directly to shareholders' equity:

	Company's share	Minority's share	Total
	N I S i n m i l l i o n s		
Increase in balance of investment property	2,527	3,722	6,249
Increase in provision for deferred taxes ⁽¹⁾	(780)	(285)	(1,065)
Increase in minority interest	-	(3,437)	(3,437)
Total increase in balance of retained earnings	1,747	-	1,747

⁽¹⁾ See note 2b.1 to the financial statements.

I. Disclosure Concerning Adoption of International Financial Reporting Standards:

The Company prepares its financial statements in accordance with generally accepted accounting principles (“GAAP”) in Israel. The Company has made arrangements to adopt International Financial Reporting Standards (“IFRS”) and is at an advanced stage in the process of preparing for the transition to reporting in accordance with IFRS. The Company is intending to make the transition to applying IFRS by early adoption, in accordance with Israel Accounting Standard No. 29, in the financial statements as of December 31, 2007; comparative data for 2006 and 2005 will be presented in the aforesaid financial statements and, hence the Company’s transition date to IFRS (hereinafter - “the transition date”) will be January 1, 2005. .

Attached in Appendix A are the reconciliations for the transition to reporting in accordance with IFRS, with regard to:

1. Effect on shareholders’ equity as of January 1, 2005, December 31, 2005 and December 31, 2006.
2. Effect on statements of income for each of the two years ended December 31, 2006.
3. Effect of transition to IFRS on the balance of retained earnings on the transition date.
4. Effect as of June 30, 2007 and for the six months ended on June 30, 2007.
5. Exemptions that the Company will take advantage of in the transition to IFRS.
6. The main differences between the accounting principles that will be applied under IFRS and the accounting principles that are applied under Israeli GAAP.

2. The Group and its Business Environment – Key Events and Changes During the Reporting Period:

General

During the reporting period, the Group's investments in the acquisition and development of new properties and in the redevelopment, expansion and construction of various other properties totaled NIS 2.5 billion. In addition, Citycon invested NIS 1 billion in acquiring and developing properties during the reporting period. The effect of these investments on the operating results will be reflected in the remainder of the year.

A. Property Activities

1. During the reporting period, the Group acquired 18 income-producing properties, with a total G.L.A. of approximately 208,000 square meters and seven plots of land for future development. The aggregate consideration for these acquisitions totaled NIS 2.1 billion.
2. During the reporting period, the Group invested a total of NIS 0.4 billion in developing new properties and in the redevelopment of existing properties.
3. As of June 30, 2007, EQY and FCR had nine properties of approximately 64,300 square meters under development, 22 properties being redeveloped and expanded and additional land reserves, which have been earmarked for future development. The total cost of these properties and land reserves totals NIS 1.1 billion. The cost to complete these development, redevelopment and expansion projects is expected to amount to a further NIS 0.8 billion.

The total cost of the properties and land as described above, which are being developed or are intended for future development, as well as the properties of Gazit Development, RSC and Gazit Europe that are being developed, is approximately NIS 1.6 billion. These properties and land did not generate any rental revenue during the reporting period.

4. As of June 30, 2007, EQY and FCR's average basic monthly rental revenue was US\$ 10.58 per square meter. During the second quarter of 2007, EQY and FCR renewed leases on 49,000 square meters, while increasing the average basic monthly rent on these leases by 13.1% to an average monthly rent of US\$ 13.44 per square meter. Additionally, the companies signed new leases on 30,000 square meters at a basic average monthly rent of US\$ 8.77 per square meter. The net operating income from the same properties increased by an average of 4.5%, compared to the corresponding period last year.

EQY's and FCR's core properties had an average occupancy rate of 94.5% as of June 30, 2007 (the rate was 95.1% as of June 30, 2006).

5. As of June 30, 2007, RSC's properties had an occupancy rate of 90.9% (the rate was 94.5% as of June 30, 2006). The average monthly rental revenue was US\$ 3,240 per unit and the NOI margin for the reporting period was 30%.

RSC has land reserves of two plots for the construction of additional senior housing communities for a total investment of US\$ 8.5 million (approximately NIS 36.1 million). The latter will consist of 471 units and the additional investment to bring them to completion is expected to be US\$ 71 million (approximately NIS 302 million).

6. As of June 30, 2007, Gazit Development's properties had an occupancy rate of 93.6% and yielded average monthly rental revenues of NIS 73.1 per square meter.

As of June 30, 2007, Gazit Development had a stake in 15 properties in Israel, as detailed below (data presented in thousands of NIS, except for rental areas):

	Qty.	Book value *	Additional investment to complete development	Rental area (square meters in thousands)
Income-producing properties	8	964,900	-	107
Properties and plots of land under development	7	366,544	480,000	118

* In accordance with Israel Accounting Standard No. 16, see section 1H above.

In addition, as of June 30, 2007, Gazit Development owns in Bulgaria an income-producing property with a G.L.A. of approximately 7,000 square meters and an office building. It also owns two plots of land in Bulgaria that are intended for the development of shopping centers and offices with an area of approximately 153,000 square meters, representing an investment of €8.8 million (approximately NIS 50.3 million). The expected additional cost of bringing these properties to completion, in a number of stages, is €20.1 million (approximately NIS 115 million), with the first stage expected to add approximately 40,000 square meters out of the total of approximately 200,000 square meters, whose development will be completed in a number of stages, as stated.

7. As of June 30, 2007, Gazit Europe's properties in Germany had an occupancy rate of 97.1% and yielded average monthly rental revenues of €11 per square meter.

As of June 30, 2007, Gazit Europe had a stake in properties in Germany, as detailed below (data presented in thousands of euros, except for rental areas):

	Qty.	Book value *	Additional investment to complete development	Rental area (square meters in thousands)
Income-producing properties	4	85,673	-	40
Properties and plots of land under development	2	12,514	75,300	38

* In accordance with Israel Accounting Standard No. 16, see section 1H above.

8. In the reporting period, Citycon invested €158.7 million (approximately NIS 900 million) in the acquisition of income-producing properties and in increasing its stake in existing shopping centers, and also in the redevelopment, at a cost of €22.7 million (approximately NIS 130 million), of income-producing properties.

The net operating income from the same properties increased by 8.8%, compared to the corresponding period last year.

As of June 30, 2007, Citycon's properties had an occupancy rate of 95.8% (the rate was 96.7% as of June 30, 2006).

As of June 30, 2007, Citycon had two properties under development at an investment of €22.5 million (approximately NIS 128 million); the expected additional cost of bringing these properties to completion is €21.4 million (approximately NIS 122 million) and their completion is expected to add approximately 22,000 square meters.

- B.** As to the issuance of capital by the Company – see note 3a to the financial statements.
- C.** As to the public debt financing by the Company by way of a shelf prospectus – see note 3c to the financial statements.
- D.** As to the placement of debentures by EQY – see note 3d to the financial statements.
- E.** As to the issuance of debentures and convertible debentures by FCR – see notes 3e, 3f and 3g to the financial statements.
- F.** As to an agreement for the provision of an unsecured credit line to FCR – see note 3h to the financial statements.
- G.** As to the issuance of capital by Citycon and the Company's participation in this issue – see note 3i to the financial statements.
- H.** As to the sale of MLS shares – see note 3b to the financial statements.

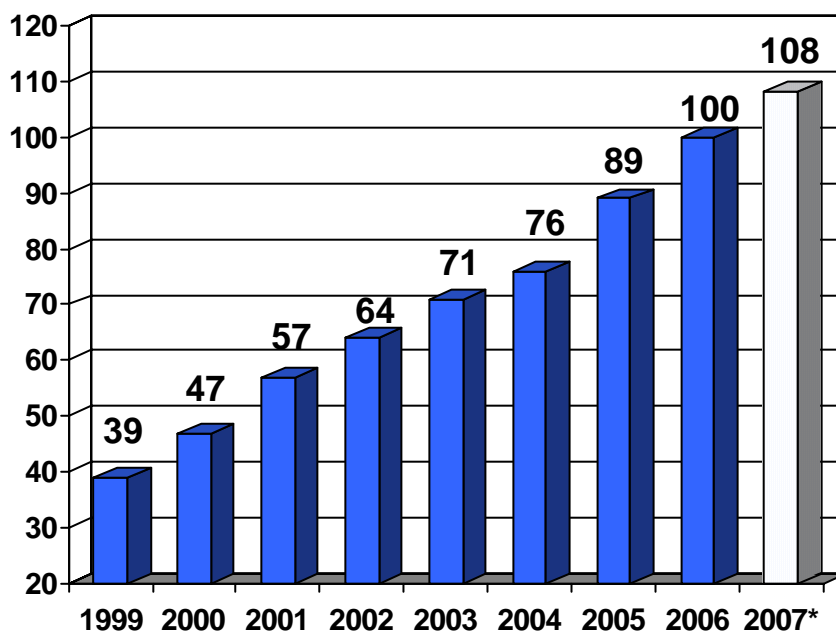
I. Dividend Distribution Policy:

Pursuant to the Company's dividend policy, the Company announces at the end of each year the anticipated dividend for the subsequent year. In November 2006, the Company decided that the dividend to be declared in 2007 would not be less than NIS 0.27 per share per quarter (NIS 1.08 per share on an annualized basis).

The above is subject to the existence of adequate amounts of distributable income at the relevant dates and is subject to the provisions of any law relating to dividend distributions and to decisions that the Company is permitted to take. This includes the appropriation of its income for other purposes and the revision of this policy.

The Company's dividend growth in the years 1999-2007 is shown in the graph below:

Agurot per share
(100 Agurot = NIS 1)



* Forecast

3. A. Results of Operations:

	For the 6 months ended June 30		For the 3 months ended June 30		For the year ended December 31,
	2007	2006	2007	2006	2006
	NIS in thousands (other than net earnings per share data)				
Property rental revenue	1,326,735	1,286,822	682,937	625,537	2,552,296
Property rental operating expenses	433,636	439,742	218,430	213,717	867,838
Property rental depreciation	4,759	226,207	2,875	113,276	453,259
Gross profit	888,340	620,873	461,632	298,544	1,231,199
Increase in fair value of investment property	502,309	-	148,711	-	-
General and administrative expenses	203,062	120,378	104,203	65,558	283,418
Operating income	1,187,587	500,495	506,140	232,986	947,781
Financing expenses, net	410,063	378,867	232,983	207,780	757,617
	777,524	121,628	273,157	25,206	190,164
Other income (expenses), net	(5,214)	324,977	2,786	317,251	514,101
Income before taxes on income	772,310	446,605	275,943	342,457	704,265
Taxes on income	131,806	48,593	49,602	24,319	84,211
Income after taxes on income	640,504	398,012	226,341	318,138	620,054
Equity in earnings of affiliates	367,225	152,799	293,732	115,127	270,566
Minority interest in earnings of subsidiaries	(404,569)	(384,059)	(152,210)	(306,801)	(529,242)
Net income	603,160	166,752	367,863	126,464	361,378
Fully diluted earnings per share	5.02	1.59	3.06	1.15	3.17
Number of shares used in computing fully diluted earnings per share (thousands of shares)	118,409	103,406	118,470	106,016	108,334

B. Analysis of Results of Operations for the First Half of 2007:

Property rental revenue

The 3% increase compared to the corresponding period last year is due to the enlargement of the property portfolio as a result of the acquisition of new properties, net of properties sold, the development properties coming on-line and the increase in the average rent per square meter received on the Group's properties. This increase was partly set-off by the changes in the average exchange rates of the Canadian dollar and the U.S. dollar between the periods.

Property operating expenses

The decrease in rental operating expenses, compared to the corresponding period last year, is mainly due to the changes in exchange rates. Rental property operating expenses, as a percentage of property rental revenue, fell to 32.7% from 34.2% for the corresponding period last year. This is mainly due to an improvement in this percentage in FCR and also to EQY's reclassification of general property operating expenses in the amount of NIS 8 million to administrative expenses.

Property depreciation

With effect from January 1, 2007, the Company applies Israel Accounting Standard No. 16 – Investment Property. As a result of implementing this standard, the Company no longer records depreciation expenses for investment property, see also section 1H above.

Gross profit

Gross profit totaled NIS 888 million (67% of property rental revenue); this compares to NIS 621 million (48.2% of property rental revenue) for the corresponding period last year – an increase of 43%. The increase in gross profit as a percentage of property rental revenue is mainly due to the implementation of Israel Accounting Standard No. 16, as explained above.

Increase in fair value of investment property

With effect from January 1, 2007, the Company applies Israel Accounting Standard No. 16 – Investment Property. As a result of implementing this standard, the Company made an adjustment, in the first half of 2007, to the fair value of its properties in the gross amount of NIS 502 million; the Company's proportionate share in this adjustment totals a gross amount of NIS 276 million, (approximately NIS 228 million, net of related taxes).

General and administrative expenses:

General and administrative expenses as a percentage of total revenues totaled 9.3%, compared to 6.8% for the corresponding period last year.

The higher percentage referred to above is mainly due to the following factors:

- 1) An increase in the Group's salary expenses as a result of taking on additional staff to cope with the growth in the Group's operations, salary expenses in respect of EQY employees that, in the past, were classified as general property operating expenses and salary expenses linked to the increase in the Company's net income.
- 2) A non-recurring charge relating to the evaluation of transactions that did not ultimately take place.
- 3) An increase in non-recurring fees to professional service providers, mainly in respect of the transition to reporting under IFRS and the valuations of investment property.

Financing expenses, net:

The change in financing expenses results from the following factors:

- 1) An increase in the Group's loans from an average balance of NIS 14.5 billion in the first half of 2006 to an average balance of NIS 17.6 billion in the first half of 2007. Interest expenses reflect an average nominal interest rate of approximately 5.8% on the Group's indebtedness, compared to 6.1% in the corresponding period last year.
- 2) The financing expenses are net of gross income of NIS 56.4 million from investments in marketable securities, which includes NIS 30.5 million from dividends, compared to NIS 38 million received in the corresponding period last year, which included NIS 29.2 million from dividends.

Other income (expenses), net

This item consists mainly of gains and losses in respect of capital transactions, such as the dilution of holdings in investee companies and real estate sales, as well as adjustments to the value of long-term investments.

As a result of the dilution of holdings in investee companies (primarily in respect of the issuance of shares and stock options and also the conversion of debentures redeemable into shares), the Company recorded a loss of NIS 3.6 million, compared to a gain of NIS 29 million in the corresponding period last year.

Additionally, EQY sold an income-producing property and three plots of land, which produced a gross gain for the Group of NIS 6.6 million (the Company's share being NIS 2.2 million), compared to the gain of NIS 393 million (the Company's share being NIS 127 million), which was mainly due to the sale of the Texas property portfolio by EQY in the corresponding period last year.

Furthermore, in the corresponding period last year, the Company wrote-down its long-term investment in MLS by a gross amount of NIS 99 million, to a price that reflected the quoted price of the shares as of June 30, 2006.

Equity in earnings of affiliates

The increase in this item is attributable to the Company's equity in the earnings of Citycon totaling NIS 363.4 million, compared to NIS 145.4 million in the corresponding period last year.

In the first half of 2007, Citycon revalued its investments in fixed assets to their fair value, in conformity with International Accounting Standard No. 40, resulting in an appreciation of €191.6 million (approximately NIS 1,056 million) in their gross value (the Company's share, net of related taxes, is approximately NIS 329 million (approximately NIS 116 million in the corresponding period last year)).

Minority interest in earnings of subsidiaries

The increase in this item mainly results from the increase in the subsidiaries' net income in respect of the first-time implementation of Israel Accounting Standard No. 16, as explained above.

C. Analysis of Results of Operations for the Second Quarter of 2007:

Property rental revenue

The 9% increase compared to the corresponding period last year is due to the enlargement of the property portfolio as a result of the acquisition of new properties, net of properties sold, the development properties coming on-line and the increase in the average rent per square meter received on the Group's properties. This increase was partly set-off by the changes in the average exchange rates of the Canadian dollar and the U.S. dollar between the periods.

Property operating expenses

The decrease in rental operating expenses, compared to the corresponding period last year, is mainly due to the changes in exchange rates. Rental property operating expenses, as a percentage of property rental revenue, fell to 32% from 34.2% for the corresponding period last year. This is mainly due to an improvement in this percentage in FCR and also to EQY's reclassification of general property operating expenses in the amount of NIS 8 million to administrative expenses.

Property depreciation

With effect from January 1, 2007, the Company applies Israel Accounting Standard No. 16 – Investment Property. As a result of implementing this standard, the Company no longer records depreciation expenses for investment property, see also section 1H above.

Gross profit

Gross profit totaled NIS 462 million (67.6% of property rental revenue); this compares to NIS 299 million (47.7% of property rental revenue) for the corresponding period last year – an increase of 55%. The increase in gross profit as a percentage of property rental revenue is mainly due to the implementation of Israel Accounting Standard No. 16, as explained above.

Increase in fair value of investment property

With effect from January 1, 2007, the Company applies Israel Accounting Standard No. 16 – Investment Property. As a result of implementing this standard, the Company made an adjustment, in the second quarter of 2007, to the fair value of its properties in the gross amount of NIS 149 million; the Company's proportionate share in this adjustment totals a gross amount of NIS 86 million, (approximately NIS 71 million, net of related taxes).

General and administrative expenses:

General and administrative expenses as a percentage of total revenues totaled 9.2%, compared to 6.2% for the corresponding period last year.

The higher percentage referred to above is mainly due to the following factors:

- 1) An increase in the Group's salary expenses as a result of taking on additional staff to cope with the growth in the Group's operations, salary expenses in respect of EQY employees that, in the past, were classified as general property operating expenses and salary expenses linked to the increase in the Company's net income.
- 2) A non-recurring charge relating to the evaluation of transactions that did not ultimately take place.
- 3) An increase in non-recurring fees to professional service providers, mainly in respect of the transition to reporting under IFRS and the valuations of investment property.

Financing expenses, net:

The change in financing expenses results from the following factors:

- 1) An increase in the Group's loans from an average balance of NIS 15 billion in the second quarter of 2006 to an average balance of NIS 18.3 billion in the second quarter of 2007. Interest expenses reflect an average nominal interest rate of approximately 5.8% on the Group's indebtedness, compared to 6% in the corresponding period last year.
- 2) The financing expenses are net of gross income of NIS 7.6 million from investments in marketable securities, which includes NIS 3.6 million from dividends, compared to NIS 5.9 million received in the corresponding period last year, which included NIS 4.3 million from dividends.

Other income (expenses), net

This item consists mainly of gains and losses in respect of capital transactions, such as the dilution of holdings in investee companies and real estate sales, as well as adjustments to the value of long-term investments.

As a result of the dilution of holdings in investee companies (primarily in respect of the issuance of shares and stock options and also the conversion of debentures redeemable into shares), the Company recorded a gain of NIS 1.5 million, compared to a gain of NIS 25.7 million in the corresponding period last year.

Additionally, EQY sold two plots of land, which produced a gross gain for the Group of NIS 2.2 million (the Company's share being NIS 0.7 million), compared to the gain of NIS 390 million (the Company's share being NIS 126 million), which was mainly due to the sale of the Texas property portfolio by EQY in the corresponding period last year.

Furthermore, in the corresponding period last year, the Company wrote-down its long-term investment in MLS by a gross amount of NIS 99 million, to a price that reflected the quoted price of the shares as of June 30, 2006.

Equity in earnings of affiliates

The increase in this item is attributable to the Company's equity in the earnings of Citycon totaling NIS 292.4 million, compared to NIS 107.7 million in the corresponding period last year.

In the second quarter of 2007, Citycon revalued its investments in fixed assets to their fair value, in conformity with International Accounting Standard No. 40, resulting in an appreciation of €160 million (approximately NIS 882 million) in their gross value (the Company's share, net of related taxes, is approximately NIS 278 million (approximately NIS 92 million in the corresponding period last year)).

Minority interest in earnings of subsidiaries

The increase in this item mainly results from the increase in the subsidiaries' net income in respect of the first-time implementation of Israel Accounting Standard No. 16, as explained above.

D. FFO and FFO per share:

The Company's practice is to publish its FFO results, which is the net reported income, after neutralizing income and expenditure of a non-recurring nature (including gains and losses resulting from the sale of properties, the adjustment of the fair value of investment property⁽¹⁾ and the changes in the percentage stake held in investee companies) and with the addition of the Company's share of depreciation of rental properties⁽²⁾ and amortization. It also publishes FFO per share results, as is already the accepted practice in those countries in which the Company operates and in accordance with the position paper issued by the NAREIT – the U.S.-based National Association of Real Estate Investment Trusts.

In addition, beginning in 2006, Israel has adopted a REIT tax regime for companies that are real estate investment trusts, similar to that in effect in various other countries throughout the world. Such companies, under certain conditions, do not pay corporate tax. The Company therefore considers that the presentation of FFO and FFO per share data, after neutralizing expenses and income in respect of deferred taxes (i.e. tax income and expenses that are not on a cash flow basis) provides a better comparison of the Company's operating results with those of other REIT companies in Israel and overseas.

According to the NAREIT position paper, the FFO (Funds From Operations) index does not represent cash flow from current operations according to accepted accounting principles, nor does it reflect the cash held by a company, or its ability to distribute that cash, and it is not a substitute for the reported net income. Furthermore, the FFO is not part of the data audited by the Company's independent auditors.

⁽¹⁾ With regard to those assets that fall within the definition of Israel Accounting Standard No. 16.

⁽²⁾ With regard to those assets that fall within the definition of Israel Accounting Standard No. 27.

The Company is of the opinion that FFO and FFO per share accurately reflect an additional aspect of the Company's operating results, providing a more appropriate basis for comparing the Company's operating results for a given period to those for previous periods and for comparing the Company's operating results to those of other property companies.

The table below presents the breakdown of the Company's FFO and FFO per share for the periods stated:

	For the 6 months ended June 30		For the 3 months ended June 30		For the year ended December 31,
	2007	2006	2007	2006	2006
NIS in thousands (other than FFO per share data)					
Net income	603,160	166,752	367,863	126,464	361,378
Adjustments to net income:					
Increase in fair value of investment property	(276,469)	-	(86,135)	-	-
Depreciation and amortization	28,751	⁽¹⁾ 202,840	6,630	⁽¹⁾ 151,602	⁽¹⁾ 231,644
Gains from dilution in holdings of consolidated subsidiaries	2,133	(28,680)	(1,606)	(25,663)	(33,301)
Losses (gains) from the sale of properties	30	(118,918)	405	(118,310)	(147,197)
Deferred tax expenses	62,911	15,643	26,508	11,615	34,863
Equity in earnings of affiliates ⁽²⁾	(367,225)	(152,799)	(293,732)	(115,127)	(270,566)
Equity in FFO of affiliates	43,556	39,376	24,755	24,882	82,190
Other adjustments ⁽³⁾	33,499	9,423	20,551	6,254	21,473
Total adjustments to FFO net income	(472,814)	(33,115)	(302,624)	(64,747)	(80,894)
FFO	130,346	133,637	65,239	61,717	240,484
Primary FFO per share (in NIS)	1.11	1.30	0.55	0.58	2.60
Fully diluted FFO per share (in NIS)	1.10	1.29	0.55	0.58	2.59
Number of shares used in computing fully diluted earnings per share (thousands of shares)	118,409	103,406	118,470	106,016	108,334

⁽¹⁾ Includes the adjustment to the value of a long-term investment. .

⁽²⁾ Includes the Company's equity in the revaluation of Citycom's investment in fixed assets to their fair value, in conformity with International Accounting Standard No. 40.

⁽³⁾ Expenses that are directly related to the income and expense items adjusted against the net income for the purpose of calculating FFO.

4. Financial Status:

Liquidity

The Group has a policy of maintaining a high level of liquidity that enables the pursuit of business opportunities in its areas of operations.

The sources of the Group's liquid assets are its cash reserves (derived from its income-producing properties), credit facilities, mortgages and long-term loans and raisings of convertible debentures and equity. As stated, these liquid assets are applied in the acquisition, development and redevelopment of income-producing assets, the settlement of liabilities, investments in affiliates, other investments and the payment of dividends.

As of June 30, 2007, the liquid assets available to the Group, including short-term investments, totaled NIS 439 million, compared to NIS 342 million as of December 31, 2006. In addition, as of June 30, 2007, the Group had unutilized credit facilities available for immediate drawdown of NIS 4.4 billion, compared to NIS 3.8 billion as of December 31, 2006.

Furthermore, as of June 30, 2007, the Group had unpledged investment property, which is carried in the books at NIS 15.3 billion.

In aggregate, the Group has cash reserves and unutilized credit facilities available for immediate drawdown totaling NIS 4.8 billion.

Current Assets

Current assets, as of June 30, 2007, totaled NIS 1 billion, compared to NIS 0.8 billion as of December 31, 2006. The increase relates mainly to the item, "cash and cash equivalents", which increased due to the sale of the MLS shares at the end of the first quarter of 2007.

Investments in Affiliates

Investments in affiliates, totaling NIS 2,151 million as of June 30, 2007, relate primarily to the investment in 76 million shares of Citycon and in convertible debentures of Citycon with a nominal value of €37 million; investments in affiliates as of December 31, 2006 totaled NIS 1,429 million. During the reporting period, the Company acquired additional Citycon shares, by means of purchases on the stock exchange and through participation in an issuance of Citycon shares, at an overall cost of NIS 326 million.

Long-Term Investments

Long-term investments, as of June 30, 2007, totaled NIS 841 million, compared to NIS 1,151 million as of December 31, 2006.

The decrease in this item is due mainly to the sale of the MLS shares at the end of the first quarter of 2007.

Investment Property, Investment Property under Development and Fixed Assets, Net

Investment property, investment property under development and fixed assets, net, as of June 30, 2007, totaled NIS 31.5 billion, compared to NIS 20.7 billion at the end of 2006. The increase is mainly due to the effect of the first-time implementation of Israel Accounting Standard No. 16 totaling NIS 6.2 billion, see also section 1H above.

During the reporting period, the Group acquired income-producing properties, developed new properties and redeveloped existing properties at a total cost of NIS 2.5 billion. In addition, the strengthening of the U.S. dollar, the Canadian dollar and the euro against the shekel at the end of the reporting period caused an increase of NIS 1.6 billion in these items.

Current Liabilities

Current liabilities, as of June 30, 2007, totaled NIS 1.8 billion, compared to NIS 1.6 billion at the end of 2006. The balance mainly consists of the line item “credit from banks and others”, which mainly consists of the current maturities of long-term liabilities in the amount of NIS 1 billion, compared to NIS 0.9 billion at the end of 2006.

The balance of current maturities includes the final settlement of loans, in the amount of NIS 0.6 billion (at the end of 2006 – NIS 0.5 billion), which are secured by a charge on the properties. Based on past experience, the Group usually renews most of these loans by taking new, long-term secured and unsecured loans.

Long-Term Liabilities

Long-term liabilities, as of June 30, 2007, totaled NIS 20.1 billion, compared to NIS 15.7 billion at the end of 2006.

The increase in this item derives principally from the issuance of debentures and the taking of new loans, which primarily financed investments in fixed assets, the acquisition of long-term investments and investments in investee companies, as well as from the increase in net deferred taxes, which rose by an amount of NIS 1.1 billion as a result of the fair value adjustment to the Company’s investment property.

Minority Interests

Minority interests, as of June 30, 2007, mainly consist of the interests of EQY’s other shareholders, who, as of June 30, 2007, accounted for 57.8% of EQY’s equity, and also the interests of FCR’s other shareholders. At the above date, FCR’s other shareholders accounted for 46.6% of FCR’s equity.

The increase in this item is due to the effect of the first-time implementation of Israel Accounting Standard No. 16, as referred to above, totaling NIS 3.4 billion and FCR’s issuance of shares during the reporting period to its shareholders. Another factor affecting the increase is the devaluation of the U.S. dollar and Canadian dollar against the shekel at the end of the reporting period, which increased the shekel amount of EQY’s and FCR’s shareholders’ equity.

Shareholders' Equity

The change in shareholders' equity, from NIS 2,865 million as of December 31, 2006, to NIS 5,510 million as of June 30, 2007, results mainly from the effect of the first-time implementation of Israel Accounting Standard No. 16, totaling NIS 1,747 million, from the income for the reporting period, totaling NIS 603 million, from the increase in the item "other capital surpluses", totaling NIS 348 million, and from the sale of treasury stock by the Company, totaling NIS 9 million. These were partly offset by the dividends of NIS 64 million paid and declared by the Company.

Shareholders' equity per share, as of June 30, 2007, totaled NIS 46.7 per share, compared to NIS 24.3 per share as of December 31, 2006. This is after a dividend distribution of NIS 0.54 per share during the reporting period.

Ratio of Debt to Total Assets

The ratio of the Group's interest-bearing debt to its gross assets (which includes accumulated depreciation in respect of fixed assets) stood at 53.8% as of June 30, 2007, compared to 63.1% as of December 31, 2006.

The ratio of the Group's interest-bearing debt to total market capitalization stood at 52.4% as of June 30, 2007, compared to 49.4% as of December 31, 2006.

The Company considers that the fair value of its assets (derived from the market value of the Group's shares) exceeds their carrying value in the Company's books and accordingly, the ratio of debt to total assets more fairly reflects the Group's leverage ratios.

Cash Flows

Cash inflows from operating activities for the reporting period and the second quarter totaled NIS 404 million and NIS 234 million, respectively, compared to NIS 338 million and NIS 183 million, respectively, for the corresponding periods last year.

In the reporting period, the Group's activities were funded by means of capital raised by the Company and its consolidated subsidiaries totaling NIS 147 million, long-term debentures and convertible debentures issued in a net amount of NIS 2,044 million, loans received and credit facilities drawn on in a net amount of NIS 169 million and long-term investments sold totaling NIS 419 million. The proceeds from the above sources were used primarily to finance investing activities for the purchase of fixed assets and investment property, which totaled NIS 2,506 million and for further investments in investee companies totaling NIS 344 million.

In the second quarter of 2007, the Group's activities were funded by means of capital raised by the Company and its consolidated subsidiaries totaling NIS 93 million and long-term debentures and convertible debentures issued in an amount of NIS 1,405 million. The proceeds from the above sources were used primarily to finance investing activities for the purchase of fixed assets and investment property, which totaled NIS 1,028 million, for the repayment of loans and credit facilities totaling NIS 849 million, for further long-term investments totaling NIS 55 million, net and for further investments in investee companies totaling NIS 18 million.

5. Donations

The Company customarily makes donations to charities and to projects for community welfare and education.

The Company makes donations to Tel-Aviv University, which has established and operates an institute focusing on research and studies of all manner of real estate-related topics (The Chaim Katzman – Gazit-Globe Real Estate Institute). In this connection, the Company has pledged to make an annual donation of US\$ 150,000 for a period of seven years.

The Company donates to the "College for All" charity – a not-for-profit organization working to close the gaps in education by means of creating equal opportunities. The organization strives to realize its vision of excellence through the provision of learning and other tools to students with ability and motivation, who come from underprivileged neighborhoods. The goal is to encourage such students into academic studies. Within the framework of this organization, the Company has pledged to provide assistance to a group of students for a period of five years.

During the reporting period, the Group's donations amounted to NIS 1.688 million.

6. Additional Information and Subsequent Events:

- A.** From the balance sheet date through the signing date of the financial statements, the Group and the affiliate invested a total of NIS 183 million in acquiring new properties and plots of land for future development. In addition, Citycon entered into a binding agreement for the acquisition of an income-producing property for €329 million.
- B.** As to the issuance of a new series of debentures by the Company – see note 4a to the financial statements.
- C.** In July and August 2007, a wholly owned subsidiary of the Company acquired – through purchases on the New York Stock Exchange (NYSE) – 2.1 million EQY shares for a consideration of US\$ 50.7 million (approximately NIS 216 million). As a result of the aforesaid acquisition, the Group's holding in EQY has risen from 42.2% to 45%.
- D.** As to the sale of MLS Preferred shares – see note 4c to the financial statements.
- E.** In July 2007, the international rating company "DBRS" raised FCR's credit rating from BBB(Low) to BBB.

7. Critical Accounting Estimates

The following is an addition to section 7 of the Directors' Report for the year ended December 31, 2006:

Changes in fair value of investment property

The Group assesses the fair value of its investment property in accordance with the provisions of Standard No. 16 of the Israel Accounting Standards Board. In determining the fair value, the Company's management relies on the valuations of independent external appraisers. Among the considerations that these appraisers take into account in making their valuations are the capitalization rates used in calculating the future cash flows from the property, the length of the lease period, the financial strength of the tenants, the amount of vacant space in the property, the length of time it takes to lease out the buildings after they become vacant, the pertinence of the rentals in properties where the rent level is above or below market rates, and the implications arising from the investments that will be required for future development.

Changes in the assumptions employed by the above external experts and by the Company's management could result in a change in the fair value, which is carried to the statement of income, and could thus affect the Company's financial position and its operating results.

8. Reporting of Exposures to Market Risks and their Management

The individuals responsible for managing and reporting the Company's market risks are Mr. Dori Segal, the Company's President, and Mr. Gil Kotler, the Company's Chief Financial Officer. Since the publication of the Company's annual report for 2006 on March 25, 2007, there have been no significant changes in the market risks or the way in which they are managed. Attached as Appendix B is the Company's linkage bases balance sheet as of June 30, 2007.

9. Disclosure Regarding Financial Statements Approval Process

The Board of Directors is the organ responsible for the overall control over the Company.

Within the framework of the process of the Company's financial statements being approved by the Board of Directors, drafts of the financial statements, directors' report and revisions to the annual periodic report are sent for the perusal of the members of the Board several days before the date of the Board meeting at which the financial statements are to be approved.

During the Board meeting, the CFO, Mr. Gil Kotler, provides a review of the Company's financial position, its operating results and its cash flows, and presents data concerning the Company's activities and their comparison with prior periods. A discussion takes place during which the Company's management reviews the major financial reporting issues that have arisen in the course of preparing the financial statements (including a review of transactions, if any, not within the normal course of business, the significant assessments and critical estimates used in the financial statements and the accounting policies applied and the changes thereto, if any) and responds to questions from the directors. The Company's independent auditors are present at Board meetings at which the financial statements are discussed and approved in order to both respond to questions, if any, raised in connection with the financial statements, and also to bring up other matters that they wish to place before the Board of Directors.

Following the aforementioned discussion, a vote is taken to approve the financial statements.

August 16, 2007

Date of Approval
of Directors' Report

Chaim Katzman

Chairman of the Board of Directors

Dori Segal

President and Director

Appendix A to the Directors' Report – Disclosure Concerning Adoption of International Financial Reporting Standards (IFRS)

1. Reconciliations of shareholders' equity:

	Note	January 1, 2005			December 31, 2005			December 31, 2006		
		Israeli GAAP	Effect of transition to IFRS	IFRS	Israeli GAAP	Effect of transition to IFRS	IFRS	Israeli GAAP	Effect of transition to IFRS (*)	IFRS
ASSETS										
CURRENT ASSETS:										
Cash and cash equivalents		52,807	-	52,807	282,212	-	282,212	194,221	118,397	312,618
Short-term investments		56,021	-	56,021	68,691	(143)	68,548	147,717	-	147,717
Derivative financial instruments	6.j	-	-	-	-	-	-	-	2,365	2,365
Tenants		103,123	-	103,123	110,732	-	110,732	132,817	5,642	138,459
Accounts receivables		125,811	(2,859)	122,952	188,952	(6,260)	182,692	210,697	33,301	243,998
Rental properties held for sale	6.f	54,888	9,215	64,103	1,298,902	487,394	1,786,296	130,739	3,346	134,085
Current tax assets	6.k	-	3,592	3,592	-	4,799	4,799	-	18,977	18,977
		<u>392,650</u>	<u>9,948</u>	<u>402,598</u>	<u>1,949,489</u>	<u>485,790</u>	<u>2,435,279</u>	<u>816,191</u>	<u>182,028</u>	<u>998,219</u>
NON-CURRENT ASSETS:										
Long-term investments	6.i	216,105	(180,001)	36,104	650,056	(616,277)	33,779	1,151,209	(1,118,556)	32,653
Long-term loans and receivables	6.a	88,687	(35,206)	53,481	116,503	(61,760)	54,743	151,432	(97,813)	53,619
Investments in available-for-sale financial assets	6.i	-	216,710	216,710	-	642,772	642,772	-	986,746	986,746
Derivative financial instruments	6.j	-	12,306	12,306	-	21,160	21,160	-	55,252	55,252
Investments in affiliates	6.e.g	533,867	2,479	536,346	721,864	630	722,494	1,429,340	(1,427,286)	2,054
Investment property	6.a	-	17,192,360	17,192,360	-	20,633,124	20,633,124	-	33,160,546	33,160,546
Investment property under development	6.a	-	317,711	317,711	-	793,902	793,902	-	1,566,790	1,566,790
Fixed assets, net	5.c	14,613,735	(14,225,572)	388,163	17,045,266	(16,807,998)	237,268	20,419,451	(20,137,790)	281,661
Goodwill	6.e	60,516	10,033	70,549	44,652	19,614	64,266	44,199	69,817	114,016
Other intangible assets, net	6.a,i	196,579	(196,225)	354	273,894	(273,502)	392	179,208	(178,787)	421
Deferred taxes	6.a,d,k	50,356	(35,529)	14,827	-	15,135	15,135	-	67,868	67,868
		<u>15,759,845</u>	<u>3,079,066</u>	<u>18,838,911</u>	<u>18,852,235</u>	<u>4,366,800</u>	<u>23,219,035</u>	<u>23,374,839</u>	<u>12,946,787</u>	<u>36,321,626</u>
<u>TOTAL ASSETS</u>		<u>16,152,495</u>	<u>3,089,014</u>	<u>19,241,509</u>	<u>20,801,724</u>	<u>4,852,590</u>	<u>25,654,314</u>	<u>24,191,030</u>	<u>13,128,815</u>	<u>37,319,845</u>

(*) Including in respect of the full consolidation of Citycon – see section 6.g below.

	Note	January 1, 2005			December 31, 2005			December 31, 2006		
		Israeli GAAP	Effect of transition to IFRS	IFRS	Israeli GAAP	Effect of transition to IFRS	IFRS	Israeli GAAP	Effect of transition to IFRS (*)	IFRS
		NIS in thousands								
EQUITY AND LIABILITIES										
CURRENT LIABILITIES:										
Credit from banks and others	6.i	755,391	(3,469)	751,922	1,291,091	(290,267)	1,000,824	966,558	483,590	1,450,148
Trade payables		152,474	-	152,474	207,621	-	207,621	195,594	25,156	220,750
Other accounts payable		256,216	(17,987)	238,229	345,404	(16,186)	329,218	402,194	168,615	570,809
Dividend declared		-	-	-	22,610	-	22,610	29,457	-	29,457
Liabilities associated with rental properties held for sale	6.f	-	-	-	-	250,610	250,610	-	-	-
Derivative financial instruments	6.j	-	6,869	6,869	-	377	377	-	18,236	18,236
Current tax liabilities	6.k	-	11,262	11,262	-	9,051	9,051	-	43,084	43,084
		<u>1,164,081</u>	<u>(3,325)</u>	<u>1,160,756</u>	<u>1,866,726</u>	<u>(46,415)</u>	<u>1,820,311</u>	<u>1,593,803</u>	<u>738,681</u>	<u>2,332,484</u>

(*) Including in respect of the full consolidation of Citycon – see section 6.g below.

	Note	January 1, 2005			December 31, 2005			December 31, 2006		
		Israeli GAAP	Effect of transition to IFRS	IFRS	Israeli GAAP	Effect of transition to IFRS	IFRS	Israeli GAAP	Effect of transition to IFRS (*)	IFRS
NIS in thousands										
NON-CURRENT LIABILITIES:										
Liabilities to financial institutions and others	6.i	7,182,308	(39,582)	7,142,726	7,951,227	(8,462)	7,942,765	7,014,366	3,524,496	10,538,862
Convertible debentures redeemable into shares of subsidiaries	6.c	479,220	2,552	481,772	351,827	(29,328)	322,499	468,134	303,117	771,251
Debentures	6.i	2,298,157	(21,150)	2,277,007	4,176,037	(49,784)	4,126,253	8,024,421	37,214	8,061,635
Linked stock options	6.b	-	13,418	13,418	-	14,693	14,693	-	1,188	1,188
Receipts from issuance of stock options in subsidiaries	6.b	-	-	-	1,284	(1,284)	-	5,909	(5,909)	-
Equity component of convertible debentures redeemable into shares of subsidiaries	6.c	-	-	-	-	-	-	19,762	(19,762)	-
Deposits from lessees and tenants		267,416	-	267,416	65,068	-	65,068	67,084	-	67,084
Derivative financial instruments	6.j	-	11,800	11,800	-	43,642	43,642	-	87,839	87,839
Employee benefits liability		1,042	-	1,042	164	-	164	259	-	259
Deferred taxes	5.a,6.a	-	671,096	671,096	85,981	883,124	969,105	168,176	1,377,603	1,545,779
Minority interest	6.h	3,458,056	(3,458,056)	-	4,395,154	(4,395,154)	-	3,963,738	(3,963,738)	-
Total non-current liabilities:		13,686,199	(2,819,922)	10,866,277	17,026,742	(3,542,553)	13,484,189	19,731,849	1,342,048	21,073,897
EQUITY:										
Issued capital		144,014	-	144,014	160,781	-	160,781	171,412	-	171,412
Share premium	6.b	922,900	(2,140)	920,760	1,409,685	31,726	1,441,411	2,071,145	52,886	2,124,031
Dividend declared subsequent to balance sheet date		17,200	-	17,200	25,419	-	25,419	31,813	-	31,813
Capital reserve for translation differences on foreign operations	5.b	124,974	(124,974)	-	257,360	(71,815)	185,545	82,620	(197,903)	(115,283)
Loans for purchase of shares		(9,418)	9,418	-	(10,818)	10,818	-	(9,844)	9,844	-
Treasury stock		(116,004)	-	(116,004)	(203,159)	-	(203,159)	(24,574)	-	(24,574)
Retained earnings		219,573	615,274	834,847	263,089	1,099,385	1,362,474	507,938	1,676,650	2,184,588
Other capital reserves	6.i,j	(1,024)	6,402	5,378	5,899	15,796	21,695	34,868	54,788	89,656
Total equity attributable to equity holders of the Company		1,302,215	503,980	1,806,195	1,908,256	1,085,910	2,994,166	2,865,378	1,596,265	4,461,643
Minority interest	6.h	-	5,408,281	5,408,281	-	7,355,648	7,355,648	-	9,451,821	9,451,821
Total equity		1,302,215	5,912,261	7,214,476	1,908,256	8,441,558	10,349,814	2,865,378	11,048,086	13,913,464
Total liabilities and equity		16,152,495	3,089,014	19,241,509	20,801,724	4,852,590	25,654,314	24,191,030	13,128,815	37,319,845

(*) Including in respect of the full consolidation of Citycon – see section 6.g below.

2. Reconciliations of income:

	Note	Year ended December 31, 2005			Year ended December 31, 2006		
		Israeli GAAP	Effect of transition to IFRS	IFRS	Israeli GAAP	Effect of transition to IFRS (*)	IFRS
		NIS in thousands (except per share amounts)					
Proport rental revenue	6.a	2,195,821	(18,717)	2,177,104	2,552,296	502,039	3,054,335
Proport rental operating expenses	6.a	717,762	(4,179)	713,583	867,838	156,220	1,024,058
Proport rental depreciation	6.a	360,800	(349,743)	11,057	453,259	(442,724)	10,535
Gross profit		1,117,259	335,205	1,452,464	1,231,199	788,543	2,019,742
Increase in fair value of investment property	6.a	-	1,187,642	1,187,642	-	2,678,091	2,678,091
General and administrative expenses		189,102	1,511	190,613	283,418	55,291	338,709
Operating income		928,157	1,521,336	2,449,493	947,781	3,411,343	4,359,124
Financing expenses	6.b,j,k	(622,058)	(128,908)	(750,966)	(757,617)	(303,698)	(1,061,315)
Financing income	6.k	-	75,304	75,304	-	114,400	114,400
Other income (expenses), net	6.a	306,099	1,467,732	1,773,831	190,164	3,222,045	3,412,209
		122,353	(61,539)	60,814	514,101	(682,201)	(168,100)
Income before taxes on income		428,452	1,409,193	1,834,645	704,265	2,539,844	3,244,109
Taxes on income	6.a,d	74,545	169,926	244,471	84,211	466,417	550,628
Income after taxes on income		353,907	1,236,267	1,590,174	620,054	2,073,427	2,693,481
Equity in earnings of affiliates	6.g	129,960	686	130,646	270,566	(234,152)	36,414
Minority interest in earnings of subsidiaries	6.g,h	(295,965)	295,965	-	(529,242)	529,242	-
Income before cumulative effect as of the beginning of the year of change in accounting principles		187,902	1,532,918	1,720,820	361,378	2,368,517	2,729,895
Cumulative effect as of the beginning of the year of change in accounting principles	6.d	(56,525)	56,525	-	-	-	-
Net income		<u>131,377</u>	<u>1,589,443</u>	<u>1,720,820</u>	<u>361,378</u>	<u>2,368,517</u>	<u>2,729,895</u>
Attributable to:							
Equity holders of the parent				615,750			938,615
Minority interest				<u>1,105,070</u>			<u>1,791,280</u>
				<u>1,720,820</u>			<u>2,729,895</u>
Net earnings per share attributable to ordinary equity holders of the Company (in NIS):							
Basic net earnings		<u>1.48</u>	<u>5.35</u>	<u>6.83</u>	<u>3.34</u>	<u>5.38</u>	<u>8.72</u>
Diluted net earnings		<u>1.40</u>	<u>5.24</u>	<u>6.64</u>	<u>3.17</u>	<u>5.24</u>	<u>8.41</u>

(*) Including in respect of the full consolidation of Citycon with effect from March 31, 2006 – see section 6.g below.

3. Data concerning the effect of the transition to IFRS on the balance of retained earnings at the transition date are presented below:

	<u>NIS in millions</u>	<u>Note</u>
Balance of retained earnings at the transition date, as presented in the financial statements under Israeli GAAP	220	
Revaluation of investment property to fair value	3,100	6.a
Taxes on revaluation of investment property	(653)	6.a,d
Minority interest in revaluation of investment property, net	(1,895)	6.a,h
Classification of adjustments arising from translation of financial statements of foreign operations	125	5.b
Share-based payments of the Company and subsidiaries	(15)	5.e
Unrealized gain on financial assets available for sale, net	(5)	6.i
Presentation as a long-term liability of options granted at fair value	(10)	6.b
Revaluation of derivative financial instruments to fair value	(*) -	6.j
Gain or loss at acquisition date of convertible debentures redeemable into shares of subsidiaries, net of related taxes	(8)	6.c
Other differences	(24)	
Total effect on the balance of retained earnings at the transition date	<u>615</u>	
Balance of retained earnings at the transition date under IFRS	<u>835</u>	

(*) Represents an amount of less than NIS 1 million.

4. Effect of the transition to IFRS for the interim period:

Presented below is an estimate of the effect of the transition to IFRS on the consolidated balance sheet as of June 30, 2007, and on the statement of income for the six-month period ended on the same date, with regard to items in the financial statements, on which the effect of the transition, in the opinion of the Company's management, is material. It is emphasized that, due to its nature of being an estimate, the information presented below could differ from the data that will actually materialize. Said information has not been reviewed or audited.

4.1 Balance sheet items:

As of June 30, 2007					
<u>Item</u>	<u>Note</u>	<u>Israeli GAAP</u>	<u>Effect of consolidation of Citycon (*)</u>	<u>Other effects of transition to IFRS</u>	<u>IFRS</u>
NIS in millions					
Asset items:					
Cash and cash equivalents		357	229	-	586
Tenants		146	13	-	159
Accounts receivable		281	41	-	322
Securities available for sale	6.i	-	-	788	788
Long-term investments	6.i	841	-	(796)	45
Long-term loans and receivables		55	-	9	64
Derivative financial instruments		-	81	56	137
Investments in affiliates	6.g	2,151	(2,147)	-	4
Investment property		29,548	10,279	-	39,827
Investment property under development		1,600	78	-	1,678
Fixed assets, net		314	4	-	318
Other assets	6.e	61	49	36	146
Total of relevant asset items		35,354	8,627	93	44,074
Liability items:					
Credit from banks and others		960	583	-	1,543
Trade payables		202	29	-	231
Other accounts payable		628	137	-	765
Liabilities to financial institutions and others		7,683	3,942	-	11,625
Debentures	6.i,j	10,426	-	(69)	10,357
Convertible debentures		511	351	-	862
Receipts from issuance of convertible options in subsidiary	6.c	29	-	(29)	-
Receipts from issuance of stock options in subsidiaries	6.b	16	-	(16)	-
Derivative financial instruments	6.j	-	11	60	71
Deferred taxes	6.a	1,427	461	3	1,891
Total of relevant liability items		21,882	5,514	(51)	27,345
Minority interest		8,049	-	(8,049)	-
Equity items:					
Share premium	6.b	2,077	-	62	2,139
Capital reserve for translation differences on foreign operations	5.b	401	-	(198)	203
Loans for purchase of shares		(9)	-	9	-
Retained earnings		2,794	-	235	3,029
Other capital reserves	6.i,j	64	-	(**) -	64
Minority interest	6.h	-	3,113	8,086	11,199
Total of relevant equity items		5,327	3,113	8,194	16,634

(*) The consolidation of Citycon, instead of its being included according to the equity method, does not have any effect on the shareholders' equity and net income attributable to the equity holders of the parent – see also section 6.g below.

(**) Represents an amount of less than NIS 1 million.

4.2 Statement of income items:

<u>Item</u>	<u>Note</u>	<u>For the six-month period ended June 30, 2007</u>			<u>IFRS</u>
		<u>Israeli</u>	<u>Effect of</u>	<u>Other</u>	
		<u>GAAP</u>	<u>consolidation</u>	<u>effects of</u>	
		<u>of Citycon</u>	<u>transition</u>		
			<u>(*)</u>	<u>to IFRS</u>	
			<u>NIS in millions</u>		
Property rental revenue		1,327	387	-	1,714
Property rental operating expenses		434	116	-	550
Property rental depreciation		5	-	-	5
Gross profit		888	271	-	1,159
Increase in fair value of investment property		502	1,056	-	1,558
General and administrative expenses		203	48	-	251
Operating income		1,187	1,279	-	2,466
Financing income (expenses), net	6.j	(410)	(107)	114	(403)
Other income (expenses), net	6.i	(5)	-	196	191
Income before taxes on income		772	1,172	310	2,254
Taxes on income	6.i	132	232	70	434
Income after taxes on income		640	940	240	1,820
Equity in earnings of affiliates		367	(363)	-	4
Minority interest in earnings of subsidiaries	6.h	(404)	(577)	981	-
Net income		603	-	1,221	1,824
Attributable to:					
Equity holders of the parent		603			840
Minority interest		-			984

(*) The consolidation of Citycon, instead of its being included according to the equity method, does not have any effect on the shareholders' equity and net income attributable to the equity holders of the parent – see also section 6.g below.

5. Exemptions to be adopted by the Company on transition to IFRS:

IFRS 1, which deals with the first-time adoption of IFRS, permits twelve exemptions whose restatement in all reporting periods prior to the transition date to IFRS is not required. The Company has elected to adopt the following exemptions:

a. Business combinations

Business combinations (IFRS 3) that took place prior to the transition date with regard to the acquisition of subsidiaries, affiliates and jointly controlled entities will not be restated.

b. Translation differences

The Company will not recognize cumulative translation differences prior to transition date for any foreign operations. The balance of the capital reserve for translation differences on foreign operations at the transition date, totaling NIS 125 million has been carried to the credit of retained earnings. As of June 30, 2007, the capital reserve will be reduced by an estimated amount of NIS 198 million, as a result of the transition to IFRS.

c. Deemed cost

The Company will present fixed assets, investment property under development and deferred charges, as of the transition date, on the basis of “deemed” cost as defined in IFRS 1. In other words, these items are presented at the reported amounts at which they were presented in the financial statements to December 31, 2004. Investment property will be presented at transition date at its fair value.

d. Embedded financial instruments

The Company does not split embedded financial instruments into their equity and liability components, with regard to liabilities that did not exist as of the transition date.

e. Share-based payment

IFRS 2, which deals with share-based payment transactions, will not be applied with regard to equity instruments granted subsequent to November 7, 2002, which had vested by the transition date.

6. The principle differences between the accounting policies to be applied in the financial statements drawn-up in accordance with IFRS and the accounting principles applied under Israeli GAAP are as follows:

a. Investment property

Under Israeli GAAP, until Accounting Standard No. 16 of the Israel Accounting Standards Board (hereinafter – “the IASB”) went into effect in January 2007, investment property was presented as part of the fixed assets according to the cost model. Pursuant to International Accounting Standard No. 40 (“IAS 40”), investment property that is held by the owner or by the lessee under a finance lease for the purpose of generating rental revenue or for capital appreciation (or for both objectives) may be presented according to the fair value model.

Furthermore, under IAS 40, a property held under an operating lease can be presented as investment property, but only if the property otherwise complies with the definition of investment property and the company applies the fair value model. Investment property under development is presented at its deemed cost until ready to generate rental revenue. Once it is ready, it is classified as investment property and measured at fair value.

The Company will apply the fair value model in its IFRS statements. The fair value has been assessed mainly on the basis of valuations performed by independent external appraisers and includes the long-term receivables and intangible assets that stem from the investment property; these balances are thus classified as part of the fair value of the investment property. Accordingly, the amount charged to investment property on the transition date totals NIS 3,100 million; against this, NIS 653 million has been added to the provision for taxes and NIS 1,895 million to minority interest, net, with the balance of NIS 552 million being added to retained earnings.

The amortization of incentives granted to tenants is recorded as a set-off against rental revenue. With effect from 2007, the transition to IFRS will not affect the financial statements, since the Company is applying Accounting Standard No. 16.

b. Stock options

Under Israeli GAAP, stock options that have an exercise price that is linked to a foreign currency (other than the company's functional currency) or to the consumer price index are presented in shareholders' equity. Under IFRS, such equity instruments are to be classified as liabilities that are measured at their fair value in each reporting period, with changes in fair value being carried to the financing item in the statement of income. When the stock options are exercised, the balance is carried to shareholders' equity. Accordingly, the balance of the liabilities in respect of linked stock options at transition date, totaling NIS 13 million, have been charged against the balance of retained earnings (NIS 10 million) and against discount on debentures (NIS 3 million), which were issued together with the stock options in a package offering. As of June 30, 2007, the Company has no liabilities in respect of linked stock options and the cumulative increase in the premium amounts to NIS 62 million.

Under Israeli GAAP, stock options issued by subsidiaries are presented between liabilities and shareholders' equity, while, under IFRS, such options are presented within the framework of the minority interest.

c. Convertible debentures redeemable into subsidiaries' shares

Under the Israeli GAAP in effect until December 31, 2005, convertible debentures redeemable into a subsidiary's shares were presented in the balance sheet as a quasi-capital instrument between long-term liabilities and shareholders' equity at the higher of their equity or capital values, when their conversion into shares was probable, and under long-term liabilities at their liability value, when their conversion into shares was not probable. Under IFRS, debentures convertible into a subsidiary's shares have to be split into their equity component, which is presented within the framework of the minority interest, and their liability component, which is presented under long-term liabilities. As part of the exemptions granted upon the first-time adoption, the aforementioned split need only be performed for debentures for which there is still a liability balance on the transition date. The balance of the equity component that is included as part of the minority interest at transition date amounts to NIS 36.3 million.

The gain or loss arising from the inter-company holding of convertible debentures redeemable into a subsidiary's shares has been charged to the statement of income on the acquisition date, in respect of the liability component of the debentures, net of related taxes.

From January 1, 2006, the date that Accounting Standard No. 22 of the IASB went into effect, the differences between Israeli GAAP and IFRS described above no longer exist.

d. Deferred tax liability in respect of a plot of land acquired in business combinations

Under Israeli GAAP, a deferred tax liability was not recognized for the temporary differences relating to a plot of land, which arose on business combinations prior to January 1, 2005. Under IFRS, the Company recognizes this liability.

e. Goodwill

Under Israeli GAAP, until Israel Accounting Standard No. 20 (Revised) of the IASB became effective on January 1, 2006, goodwill that arose on business combinations was systematically amortized over a period of up to 20 years. Since the above date, goodwill is not written down except in the event of its impairment. Under IFRS 3, including the exemption permitted upon its implementation by virtue of IFRS 1, the amortization of goodwill is discontinued with effect from the transition date, subject to review for impairment. As a result of recognizing business combinations in accordance with IFRS 3, pursuant to which investment property is presented at fair value, the balance of goodwill as of June 30, 2007 will increase by an estimated amount of NIS 36 million.

f. Assets held for sale and discontinued operations

Under Israeli GAAP, there is no requirement for assets held for sale to be measured differently. Under IFRS 5, an asset held for sale is presented separately and is to be measured at the lower of its carrying value or its fair value, less costs of sale, and depreciation or amortization is not to be included for such an asset.

g. Consolidation of the financial statements

In the financial statements drawn up in accordance with IFRS, the Company applies the IASB's statement regarding tests for the existence of effective control. Accordingly, in its financial statements drawn up in accordance with IFRS, the Company will consolidate both EQY and Citycon (Citycon has been consolidated commencing from the end of the first quarter of 2006 in accordance with when the particular circumstances existed that testify to effective control having been obtained). However, in the financial statements drawn up in accordance with Israeli GAAP, the Company only consolidates EQY on the basis of effective control, with this being in line with the approach of the Israel Securities Authority, which distinguishes between effective control after dilution of formal control and effective control without there ever having been formal control previously.

Under Israeli GAAP, potential voting rights are not taken into account when assessing whether control is exerted over a company. Pursuant to International Accounting Standard No. 27, the effect of potential voting rights exercisable at balance sheet date has been taken into account.

h. Minority interest

Under Israeli GAAP, the minority interest is presented in the balance sheet outside the framework of shareholders' equity, while under IFRS, the minority interest is presented as part of the equity. Accordingly, under Israeli GAAP, the minority's share in the results of subsidiaries is included as part of the results in the income statement, while under IFRS, the minority's share in the results is not included in the income statement, but is presented as part of the attribution of earnings to the shareholders.

The increase in the minority interest at the transition date, amounting to NIS 1,950 million, stems from the increase in the minority's share in the shareholders' equity of subsidiaries, due primarily to the presentation of investment property at fair value, amounting to NIS 1,895 million (net of related taxes). The increase in the minority interest as of June 30, 2007 is due to the reason explained above and to an additional increase in respect of the consolidation of Citycon (see 6.g above) amounting to NIS 3.1 billion.

i. Financial instruments

Under Israeli GAAP, the Company presents its investment in marketable securities that fall within the definition of a “permanent investment” at cost, net of any impairment that is not of a temporary nature, while securities that are included as a “current investment” are presented at their fair value, with changes in the valuation being carried to income. On the other hand, under International Accounting Standard No. 39, the Company presents its investments in financial instruments available for sale at their fair value, with valuation differences being carried to capital reserve, except in the case of an impairment, which is charged to the statement of income. The increase in the item “securities available for sale”, which is charged against capital reserve, amounted to NIS 13 million at transition date, and includes NIS 5 million in respect of an unrealized gain that has been charged against the balance of retained earnings. As of June 30, 2007, the capital reserve from revaluation is estimated to amount to NIS 0.1 million in debit, and the balance charged to the debit of retained earnings in respect of the unrealized gain amounts to NIS 1.3 million.

In the financial statements before the application of IFRS, the Company will recognize income of NIS 196 million (NIS 126 million, net of related taxes) in the reporting period, as a result of canceling the impairment allowance in respect of the investment in MLS.

Financial liabilities – Under Israeli GAAP, the Company applies Israel Accounting Standard No. 22 with effect from January 1, 2006, whereby the discount, premium and deferred expenses relating to obtaining loans, are amortized according to the effective interest method and are presented as a deduction from the balance of the liability. Under International Accounting Standard No. 32, this policy is applied from the date of the assumption of the liability, and thus deferred expenses have been removed from “other assets” and reclassified as a reduction of the balance of liabilities.

j. Derivative financial instruments

Under IFRS, derivative financial instruments are initially recognized at fair value and this is remeasured at each reporting date. Gains or losses during the year arising from changes in the fair value of the derivatives, where these do not meet the criteria for hedge accounting, are carried immediately to income, as explained below:

Cash flow hedges - Under Israeli GAAP, the results of the intrinsic value of a derivative financial instrument that meets the criteria of a hedge instrument are deferred and are recognized in the income statement concurrently with the result of the hedged item. Under International Accounting Standard No. 39, the effective portion of the gain or loss resulting from the change in the fair value of the hedge instrument is recognized directly in shareholders’ equity, while the ineffective portion is immediately recognized in the statement of income.

Hedges of a net investment - Under Israeli GAAP, the intrinsic value of an instrument hedging a net investment in a foreign operation is carried to the capital reserve for translation differences on foreign operations. Under International Accounting Standard No. 39, the hedging of a net investment in foreign operations, including a hedge of a monetary item that is reported as part of the net investment, is reported in a similar fashion to a cash flow hedge. The effective portion of gains or losses resulting from a change in the fair value of the hedge instrument is carried to shareholders' equity, while gains or losses deriving from the ineffective portion of the hedge are charged to the statement of income. In instances where documentation does not exist to assign the derivative to the objectives of the hedge and to examine the effectiveness of the hedge, the derivative cannot be recognized as a hedge instrument.

As of June 30, 2007, an amount of NIS 64 million, which had been credited to the debentures, pursuant to Israeli GAAP, as a result of measuring the intrinsic value of the exchange transactions, has been reclassified to the item "derivative financial instruments" in the balance sheet. As of June 30, 2007, the balance of the fair value of the exchange transactions is estimated to amount to NIS 137 million (on the assets side) and to NIS 71 million (on the liabilities side). As a result of recognizing these transactions at fair value, financing expenses have been reduced by an estimated amount of NIS 114 million in the reporting period. The Company's share in the capital reserve for the revaluation of exchange transactions to fair value in subsidiaries amounts to NIS 50 million (in credit) as of June 30, 2007.

k. Financial statements presentation

In accordance with the provisions of IAS 1, the presentation rules will be applied in the financial statements, pursuant to which:

- Liabilities and assets in respect of deferred taxes are recorded only as long-term balances.
- Liabilities and assets in respect of current taxes are presented separately in the balance sheet.
- Financing income and expenses are presented separately in the statement of income.

Appendix B to the Directors' Report

Linkage Bases Balance Sheet

as of June 30, 2007

	Linked to the consumer price index	In US\$ or linked thereto	In C\$ or linked thereto	In unlinked NIS	In euros	Unlinked	Total
N I S i n t h o u s a n d s							
Monetary assets							
Cash and cash equivalents	-	71,096	250,160	10,871	24,529	-	356,656
Short-term investments	-	25,441	5,201	-	-	51,751	82,393
Tenants, accounts receivable and other debit balances	31,296	103,432	168,111	6,721	32,299	85,695	427,554
Investments in affiliates	-	-	-	-	214,627	-	214,627
Long-term investments	3,802	27,449	14,197	-	-	795,881	841,329
Long-term loans and debit balances	5,436	38,856	10,419	-	-	-	54,711
	40,534	266,274	448,088	17,592	271,455	933,327	1,977,270
Non-monetary assets⁽¹⁾	-	14,174,029	15,366,584	1,477,282	2,493,730	60,884	33,572,509
	40,534	14,440,303	15,814,672	1,494,874	2,765,185	994,211	35,549,779
Liabilities							
Short-term credit from banks and others	-	2,868	-	-	-	-	2,868
Trade and other payables and other credit balances	16,797	289,539	368,823	147,622	20,318	18,946	862,045
Debentures	1,773,906	4,491,876	3,363,767	794	863,713	-	10,494,056
Liabilities to financial institutions and others	169,012	3,299,957	4,819,464	-	282,723	-	8,571,156
Deposits from tenants	2,529	44,636	31,260	-	-	-	78,425
Liabilities for employee rights upon retirement	-	-	-	222	-	-	222
Deferred taxes	-	-	-	-	-	1,426,470	1,426,470
Convertible debentures redeemable for subsidiary's shares	-	-	511,304	-	-	-	511,304
	1,962,244	8,128,876	9,094,618	148,638	1,166,754	1,445,416	21,946,546
Receipts in respect of subsidiary's convertible options	-	-	28,824	-	-	-	28,824
Receipts from issue of subsidiaries' stock options	-	7,848	7,860	-	-	-	15,708
Minority interests	-	-	-	-	-	8,048,933	8,048,933
Shareholders' equity	-	-	-	-	-	5,509,768	5,509,768
	1,962,244	8,136,724	9,131,302	148,638	1,166,754	15,004,117	35,549,779

⁽¹⁾ Mainly investment property and investment property under development.