

Translation from Hebrew

DBS SATELLITE SERVICES (1998) LTD.
CONDENSED INTERIM FINANCIAL STATEMENTS
AS OF MARCH 31, 2004
(Unaudited)

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Translation from Hebrew

May 24, 2004

The Board of Directors of
DBS Satellite Services (1998) Ltd.
6 Hayozma Street
Kfar Saba Industrial Zone

Dear Sirs,

Re: Review of unaudited condensed interim financial statements for
the period ended March 31, 2004

At your request, we have reviewed the condensed interim balance sheet of DBS Satellite Services (1998) Ltd. (hereafter – the Company) as of March 31, 2004 and the condensed interim statements of operations, changes in capital deficiency and cash flows for the three month period then ended. Our review was performed in accordance with the procedures prescribed by the Institute of Certified Public Accountants in Israel. Inter alia, these procedures include: reading of the aforementioned financial statements, reading of minutes of meetings of shareholders and of the board of directors and its committees, and making inquiries of officers responsible for financial and accounting matters.

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

During our review, nothing came to our attention that indicated that significant changes should be made in the aforementioned condensed statements in order for them to be considered as drawn up in conformity with generally accepted accounting principles and the Israeli Securities Regulations (Periodic and Immediate Reports), 1970.

We draw attention to note 4 regarding the financial position of the Company and the financing agreements with banks and with the Company's shareholders, including the non-compliance with some of the terms stipulated in such agreements. As explained in the abovementioned note, the Company's activity depends on the continuing receipt of additional loans from shareholders under the financing agreements, including loans from the principal shareholder in accordance with the Company's operating plan.

This review report is based on the previous review report on the financial statements for the aforesaid period, which was issued on May 16, 2004. We consent to this review report being included in the prospectus of "Bezeq" The Israel Telecommunication Corp. Ltd., which is intended to be published in May 2004.

Sincerely yours,

DBS SATELLITE SERVICES (1998) LTD.CONDENSED BALANCE SHEET
AS OF MARCH 31, 2004

	March 31		December 31,
	2004	2003	2003
	(Unaudited)		(Audited)
	In thousands (see note 3)		
A s s e t s			
CURRENT ASSETS:			
Cash and cash equivalents		1,955	
Short-term deposit	1,845	2,718	1,834
Accounts receivable:			
Trade	99,176	98,439	99,992
Other	5,069	4,492	5,362
T o t a l current assets	<u>106,090</u>	<u>107,604</u>	<u>107,188</u>
BROADCASTING RIGHTS:			
Cost	240,424	287,794	250,162
Less - utilized rights	111,700	128,597	121,828
	<u>128,724</u>	<u>159,197</u>	<u>128,334</u>
FIXED ASSETS:			
Cost	2,168,364	1,974,337	2,109,436
Less - accumulated depreciation	1,083,638	692,406	985,278
	<u>1,084,726</u>	<u>1,281,931</u>	<u>1,124,158</u>
	<u>1,319,540</u>	<u>1,548,732</u>	<u>1,359,680</u>
Liabilities, net of capital deficiency			
CURRENT LIABILITIES:			
Bank credit (see note 4)	1,304,846	1,159,445	1,304,660
Accounts payables and accruals:			
Trade	507,302	502,324	470,075
Other	95,148	76,184	87,668
T o t a l current liabilities	<u>1,907,296</u>	<u>1,737,953</u>	<u>1,862,403</u>
LONG-TERM LIABILITIES:			
Liability for employee rights upon retirement	4,404	3,255	4,143
Customer deposits – net	14,007	38,465	18,238
Other liabilities, net of current maturities	3,591	29,555	9,477
T o t a l long-term liabilities	<u>22,002</u>	<u>71,275</u>	<u>31,858</u>
SHAREHOLDERS' LOANS	<u>2,306,469</u>	<u>2,110,173</u>	<u>2,271,283</u>
T o t a l liabilities	<u>4,235,767</u>	<u>3,919,401</u>	<u>4,165,544</u>
CAPITAL DEFICIENCY	<u>(2,916,227)</u>	<u>(2,370,669)</u>	<u>(2,805,864)</u>
	<u>1,319,540</u>	<u>1,548,732</u>	<u>1,359,680</u>

Ilan Biran
Chairman of the
Board of Directors

Ofer Bloch
Chief Executive Officer

Katriel Moriah
VP Finance

Date of approval of the financial statements: May 24, 2004.

The accompanying notes are an integral part of these condensed financial statements.

Translation from Hebrew

DBS SATELLITE SERVICES (1998) LTD.
CONDENSED STATEMENT OF OPERATIONS
FOR THE 3 MONTH PERIOD ENDED MARCH 31, 2004

	3 months ended		Year ended
	March 31		December 31,
	2004	2003	2003
	(Unaudited)		(Audited)
	In thousands (see note 3)		
REVENUES	235,788	193,934	842,374
OPERATING EXPENSES	262,247	250,564	1,012,159
GROSS LOSS	26,459	56,630	169,785
SELLING, MARKETING, GENERAL AND ADMINISTRATIVE EXPENSES:			
Selling and marketing	27,889	24,899	109,859
General and administrative	18,792	21,448	84,691
	46,681	46,347	194,550
LOSS FROM ORDINARY OPERATIONS	73,140	102,977	364,335
FINANCIAL EXPENSES (INCOME), net	35,836	14,355	179,608
OTHER EXPENSES	1,387	2,610	11,201
LOSS FOR THE PERIOD	110,363	119,942	555,144

The accompanying notes are an integral part of these condensed financial statements.

DBS SATELLITE SERVICES (1998) LTD.
CONDENSED STATEMENT OF CHANGES IN CAPITAL DEFICIENCY
FOR THE 3 MONTH PERIOD ENDED MARCH 31, 2004

	Share capital and premium	Accumulated deficit	Total
	In thousands (see note 3)		
BALANCE AS OF JANUARY 1, 2004 (audited)	27	(2,805,891)	(2,805,864)
CHANGES DURING THE 3 MONTHS ENDED MARCH 31, 2004 (unaudited) -			
Loss		(110,363)	(110,363)
BALANCE AS OF MARCH 31, 2004 (unaudited)	<u>27</u>	<u>(2,916,254)</u>	<u>(2,916,227)</u>
BALANCE AS OF 1 JANUARY, 2003 (audited)	20	(2,250,747)	(2,250,727)
CHANGES DURING THE 3 MONTHS ENDED MARCH 31, 2003 (unaudited) -			
Loss		(119,942)	(119,942)
BALANCE AS OF MARCH 31, 2003 (unaudited)	<u>20</u>	<u>(2,370,689)</u>	<u>(2,370,669)</u>
BALANCE AS OF JANUARY 1, 2003 (audited)	20	(2,250,747)	(2,250,727)
CHANGES DURING THE YEAR ENDED DECEMBER 31, 2003 (audited):			
Issuance of share capital	7		7
Loss		(555,144)	(555,144)
BALANCE AS OF DECEMBER 31, 2003 (audited)	<u>27</u>	<u>(2,805,891)</u>	<u>(2,805,864)</u>

The accompanying notes are an integral part of these condensed financial statements.

DBS SATELLITE SERVICES (1998) LTD.
CONDENSED STATEMENT OF CASH FLOWS
FOR THE 3 MONTH PERIOD ENDED MARCH 31, 2004

	3 months ended		Year ended
	March 31		December31,
	2004	2003	2003
	(Unaudited)		(Audited)
	In thousands (see note 3)		
CASH FLOWS FROM OPERATING ACTIVITIES:			
Loss for the period	(110,363)	(119,942)	(555,144)
Adjustments required to reflect the cash flows from operating activities (a)	165,712	125,334	552,127
Net cash provided by (used in) operating activities	55,349	5,392	(3,017)
CASH FLOWS FROM INVESTING ACTIVITES, see (b) below:			
Short-term deposit			955
Payments on account of the purchase of fixed assets	(53,281)	(78,827)	(299,894)
Payments on account of the purchase of broadcasting rights	(36,614)	(50,276)	(118,551)
Proceeds from sale of fixed assets	1,875	3,283	14,130
Net cash used in investing activities	(88,020)	(125,820)	(403,360)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Issuance of share capital			7
Receipt of long-term loans from shareholders	32,485	65,663	204,433
Short-term bank credit - net	186	55,072	200,289
Net cash provided by financing activities	32,671	120,735	404,729
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS			
	-	307	(1,648)
BALANCE OF CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD			
	-	1,648	1,648
BALANCE OF CASH AND CASH EQUIVALENTS AT END OF PERIOD			
	-	1,955	-

DBS SATELLITE SERVICES (1998) LTD.
CONDENSED STATEMENT OF CASH FLOWS
FOR THE 3 MONTH PERIOD ENDED 31 MARCH, 2004

	3 months ended		Year ended
	March 31		December 31,
	2004	2003	2003
	(Unaudited)		(Audited)
	In thousands (see note 3)		
(a) Adjustments required to reflect the cash flows from operating activities:			
Income and expenses not involving cash flows:			
Depreciation and amortization	96,165	97,407	384,873
Utilized broadcasting rights	32,066	31,745	132,549
License depreciation			6,362
Depreciation of installation equipment	750		4,654
Liability for employee rights upon retirement, net	261	468	1,357
Linkage differences on principal of other long-term liability		592	
Linkage differences on (erosion of) principal of long-term shareholders' loans	2,701	(7,446)	14,893
Other	626	(112)	1,424
	<u>132,569</u>	<u>122,654</u>	<u>546,112</u>
Changes in operating asset and liability items:			
Decrease (increase) in accounts receivable:			
Trade	(1,028)	3,117	(2,925)
Other	293	262	(608)
Increase (decrease) in accounts payable and accruals:			
Trade	30,629	3,298	22,288
Customer deposits, net	(4,870)	(2,625)	(23,203)
Other	8,119	(1,372)	10,463
	<u>33,143</u>	<u>2,680</u>	<u>6,015</u>
	<u>165,712</u>	<u>125,334</u>	<u>552,127</u>
(b) Supplementary information on investment activities not involving cash flows			
Increase (Decrease) in suppliers' credit for purchase of fixed assets	<u>4,870</u>	<u>(17,930)</u>	<u>(90,324)</u>
Increase (Decrease) in suppliers' credit for purchase of broadcasting rights	<u>(4,158)</u>	<u>3,745</u>	<u>5,143</u>

The accompanying notes are an integral part of these condensed financial statements.

DBS SATELLITE SERVICES (1998) LTD.

NOTES TO CONDENSED FINANCIAL STATEMENTS

AS OF MARCH 31, 2004

(Unaudited)

1. General

The interim financial statements as of March 31, 2004 and for the three month period then ended (hereafter - the interim statements) were drawn up in condensed form, in accordance with Accounting Standard No. 14 of the Israel Accounting Standards Board (hereafter - the IASB) and in accordance with the Securities (Periodic and Immediate Reports) Regulations, 1970. The generally accepted accounting principles applied in preparation of the interim statements are consistent with those applied in preparation of the annual financial statements; nevertheless, the interim statements do not include all the information and notes which are required for annual financial statements.

2. Activities

DBS Satellite Services (1998) Ltd. (hereafter - the Company) was incorporated in Israel on December 2, 1998. In January 1999, the Company received a license from the Ministry of Communications to broadcast in Israel television broadcasts by means of satellite (hereafter - the License). The License is for a period of ten years from the date of its receipt, and can be extended for an additional period of six years, subject to certain conditions. In June 2002, the License was extended by five years.

The Company is subject to the Telecommunications Law, 1982 (hereafter - the Telecommunications Law), the regulations and rules promulgated thereunder and the terms of the License.

In July 2000, the Company completed the development stage and began to provide its customers with multi-channel television broadcasts in accordance with the License granted to it under the Telecommunications Law.

- 3.** With effect from January 1, 2004, the company has adopted the provisions of Standard No. 12 – “Discontinuance of Adjusting Financial Statements for Inflation” – of the IASB and, pursuant thereto, the company has discontinued, from the aforesaid date, the practice of adjusting its financial statements for the effects of inflation.

Through December 31, 2003, the company prepared its financial statements on the basis of historical cost adjusted for the changes in the general purchasing power of Israeli currency (hereafter – “NIS”), based upon changes in the consumer price index (hereafter – “the CPI”), in accordance with pronouncements of the Institute of Certified Public Accountants in Israel (hereafter – “the Israeli Institute”). The adjusted amounts, as above, presented in the financial statements as of December 31, 2003 (hereafter – “the transition date”), are used as the opening balances for the nominal-historical financial reporting in the following periods. Additions made after the transition date have been included in the financial statements at their nominal values.

The amounts reported for periods after the transition date are composed as follows: all the amounts originating from the period prior to the transition date are composed of their adjusted amount at the transition date, with the addition of amounts in nominal values that were added after the transition date, and net of amounts that were deducted after the transition date (the retirement of such sums is effected at their adjusted values as of transition date, their nominal values, or a combination of the two, according to the circumstances). All the amounts originating from the period after the transition date are included in the financial statements at their nominal values.

DBS SATELLITE SERVICES (1998) LTD.

NOTES TO CONDENSED FINANCIAL STATEMENTS (continued)

AS OF MARCH 31, 2004

(Unaudited)

4. The Company's financial position:

- a) Since the commencement of its activities, the Company has incurred significant losses, which are accompanied by negative cash flows from operating activities. The loss for 2003 amounts to approximately adjusted NIS 555 million and the loss for the 3 month period ended 31 march, 2004 amounts to approximately NIS 110 million. As a result of these losses, the Company's capital deficiency and working capital deficiency as of march 31, 2004 amounted to approximately adjusted NIS 2,916 million and adjusted NIS 1,801 million, respectively. The working capital deficiency includes approximately adjusted NIS 1,305 million in credit from banks (see also (b) below).
- b) On May 23, 2001, the Company signed a financing agreement (hereafter - the financing agreement) with certain banks (hereafter - the Banks). The financing agreement includes, inter alia, undertakings by the Company to meet certain suspending conditions as well as specified cumulative milestones and financial stipulations (hereafter - the terms).

On December 30, 2002, the Company, its shareholders and the Banks signed an agreement regarding the expansion of the credit facility provided by the Banks (hereafter - the interim facility), which is to be carried out in parallel with additional investments by the shareholders, in an amount not less than 150% of the amount infused by the Banks. Receipt of the finance under the interim facility is, inter alia, conditional upon the Company's meeting certain financial and operating conditions, as stipulated in said agreement.

To date of approval of these financial statements, the shareholders and the Banks have transferred the Company the full amount of their share under the interim facility. Despite this, some of the terms stipulated in the financing agreement and the interim facility was not fulfilled.

At the same time as the aforesaid agreement was being signed, discussions were being held between the parties regarding the expansion of the interim facility within the framework of an amendment to the financing agreement (hereafter - the amendment agreement).

A financial review completed by the Banks in March 2003 determines that the overall amount of finance required for the Company does not exceed the amount of the interim facility, together with the addition thereto provided under the amendment agreement (including the shareholders' proportionate share).

On August 6, 2003, the Banks and the Company signed the amendment agreement. Pursuant to the amendment agreement, the Banks are to provide the Company with further facilities, in addition to those provided under the financing agreement and the interim facility, this being subject to the Company complying with the conditions and achieving the milestones stipulated in the amendment agreement which include the shareholders making additional investments amounting to not less than 150% of the amount to be infused by the Banks.

DBS SATELLITE SERVICES (1998) LTD.

NOTES TO CONDENSED FINANCIAL STATEMENTS (continued)

AS OF MARCH 31, 2004

(Unaudited)

4. The Company's financial position (continued):

The amendment agreement became effective in December 2003. To the date of the approval of the financial statements, the Company is not in full compliance with said conditions and, consequently, the Banks have not provided the Company with the amounts that were to have been made available to it during the first quarter of 2004 under this agreement. The Company is negotiating an agreement with the Banks that will further revise the conditions with which the Company will have to comply in the amendment agreement (see note c).

Pursuant to the amendment agreement, the Company converted short-term credit in the amount of NIS 1,225 million into long-term loans in February 2004. Within the framework of these financial statements, the long-term loans are presented among the Company's current liabilities, as the Company is not in compliance with some of the suspending conditions stipulated in the amendment agreement.

- c) On March 9, 2004, the Company's board of directors approved a framework for a multi-year operating plan in respect of the years 2004 and 2005 (hereafter – "the operating plan"), inter alia, following a report commissioned by the principal shareholder from an external financial consultant with regard to the Company's business situation. The financial report reveals that the Company's financing requirements for the above years will exceed those stipulated under the amendment agreement. Pursuant to the operating plan approved by the board of directors as stated above, the Company will require significantly greater external financing during the aforementioned years, than that stipulated under the amendment agreement.

On March 30, 2004, the principal shareholder's board of directors approved an additional investment (in excess of its share under the amendment agreement) in the amount of NIS 440 million through to the end of 2005. This amount will be invested in stages in accordance with the Company's requirements under the operating plan. The principal shareholder's board of directors also agreed to bring forward and immediately invest the balance of its investment due under the amendment agreement. Pursuant to this decision, the additional investment that was approved as stated above is to be made taking into account the following factors: the shareholder's satisfaction with developments in the regulation of the communications market, the continued provision of financing by the Banks in accordance with their share of the amendment agreement, the receipt of the necessary approvals, and the response of the Attorney General (see d. below).

- d) The receipt of additional loans from a principal shareholder was conditional (subject to the shareholder's position as a government company), inter alia, upon the approval of the Ministerial Committee for Privatization (hereafter - the Committee), this by virtue of the terms stipulated in the approval that the Committee has granted to the principal shareholder to invest in the Company. At the time, the Committee has given approval for the shareholder to increase his investment up to the sum arrived at by multiplying the percentage of his holding in the Company's share capital by U.S. \$ 600 million.

DBS SATELLITE SERVICES (1998) LTD.

NOTES TO CONDENSED FINANCIAL STATEMENTS (continued)

AS OF MARCH 31, 2004

(Unaudited)

4. The Company's financial position (continued):

The Government Companies Authority has notified the principal shareholder that the deputy attorney general has confirmed that no further approval of the Committee will be required for the increased investment in the Company by the principal shareholder.

- e) The Company's activity depends on the receipt of additional loans from shareholders under the financing agreements, including loans from the principal shareholder in accordance with the Company's operating plan, see also (c) and (d) above.
The Company's management believes that there is a good chance that all the financing resources required for the coming year will be arranged.

5. Data regarding the changes in the exchange rate of the U.S. dollar (hereafter - the dollar) and in the consumer price index:

	<u>Exchange rate of the dollar</u>	<u>Consumer price index</u>
Three months ended March 31:		
2004	3.4%	(0.1%)
2003	(1.06%)	0.8%
Year ended December 31, 2003	(7.6%)	(1.9%)