ELRON ELECTRONIC INDUSTRIES LTD.

AND ITS SUBSIDIARIES

CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

As of June 30, 2006

(Unaudited)

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AND ITS SUBSIDIARIES

CONDENSED INTERIM CONSOLIDATED

FINANCIAL STATEMENTS

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UNAUDITED

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CONSOLIDATED BALANCE SHEETS

U.S. dollars in thousands, except share and per share data

	June 30, 2006 Unaudited	December 31, 2005
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$ 38,290	$ 26,520
Short-term investments	25,684	54,661
Available-for-sale marketable debentures	58,685	62,617
Trade receivables (net of allowance for doubtful accounts of $5 and of $426 at June 30, 2006 and at December 31, 2005)*	6,399	6,440
Other receivables and prepaid expenses*	2,730	2,846
Inventories	2,069	2,117
Total current assets	133,857	155,201
INVESTMENTS AND LONG-TERM RECEIVABLES		
Investments in affiliated companies	97,633	102,780
Investments in other companies and long-term receivables*	82,063	73,931
Deferred taxes	6,374	6,521
Severance pay deposits	2,290	1,971
Total investments and long-term receivables	188,360	185,203
PROPERTY AND EQUIPMENT, NET	8,043	7,809
INTANGIBLE ASSETS		
Goodwill	2,742	2,742
Other intangible assets	2,809	2,818
Total intangible assets	5,551	5,560
Total assets	$ 335,811	$ 353,773

* Includes short term receivables from related parties in the aggregate amount of $5,158 and $5,043 as of June 30, 2006 and December 31, 2005, respectively, and long term receivables from related parties in the aggregate amount of $450 and $434 as of June 30, 2006 and December 31, 2005, respectively.

The accompanying notes are an integral part of the consolidated financial statements.

CONSOLIDATED BALANCE SHEETS

U.S. dollars in thousands, except share and per share data

	June 30, 2006	December 31, 2005
	Unaudited	
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES		
Short-term loans from banks	$ 700	$ 3,808
Current maturities of long-term loans from banks and others	2,141	2,065
Trade payables	2,335	2,146
Other payables and accrued expenses	11,475	11,025
Total current liabilities	16,651	19,044
LONG-TERM LIABILITIES		
Long-term loans from banks and others	3,439	1,477
Accrued severance pay and retirement obligations	3,179	2,635
Deferred taxes	8,343	9,494
Total long-term liabilities	14,961	13,606
MINORITY INTEREST	12,777	19,007
SHAREHOLDERS' EQUITY:		
Ordinary shares of NIS 0.003 par value; Authorized - 35,000,000 shares as of June 30, 2006 and December 31, 2005; Issued and outstanding – 29,531,955 and 29,483,455 shares as of June 30, 2006 and as of December 31, 2005, respectively.	9,572	9,572
Additional paid-in capital	271,564	271,132
Accumulated other comprehensive income	9,553	10,741
Retained earnings	733	10,671
Total shareholders' equity	291,422	302,116
Total liabilities and shareholders' equity	$ 335,811	$ 353,773

The accompanying notes are an integral part of the consolidated financial statements.

CONSOLIDATED STATEMENTS OF OPERATIONS

U.S. dollars in thousands, except share and per share data

	Six months ended June 30, 2006	Six months ended June 30, 2005***	Three months ended June 30, 2006	Three months ended June 30, 2005***	Year ended December 31, 2005
	Unaudited				
INCOME					
Net revenues*	$ 7,138	$ 6,246	$ 3,816	$ 3,261	$ 12,646
Equity in losses of affiliated companies	(11,866)	(7,827)	(8,371)	(4,244)	(17,522)
Gain (loss) from disposal of businesses and affiliated companies and changes in holdings in affiliated companies, net	(7)	22,389	(23)	22,399	23,328
Other income, net	3,367	56,533	738	56,255	58,648
Financial income, net	2,280	4,267	1,196	3,370	5,483
	912	81,608	(2,644)	81,041	82,583
COSTS AND EXPENSES					
Cost of revenues	3,862	3,960	2,017	2,085	7,907
Research and development costs, net	5,878	2,643	2,970	1,409	6,163
Marketing and selling expenses, net	2,128	1,089	1,253	620	2,386
General and administrative expenses	5,911	4,248	3,030	2,296	9,249
Amortization of intangible assets	9	145	4	110	392
	17,788	12,085	9,274	6,520	26,097
Income (loss) before taxes on income	(16,876)	69,523	(11,918)	74,521	56,486
Tax benefit (Taxes on income)	(99)	(25,867)	183	(26,034)	(10,461)
Income (loss) after taxes on income	(16,975)	43,656	(11,735)	48,487	46,025
Minority interest in losses of subsidiaries	7,037	645	5,310	451	5,160
Income (loss) from continuing operations	(9,938)	44,301	(6,425)	48,938	51,185
Loss from discontinued operations**	-	(2,214)	-	(1,738)	(3,850)
Net income (loss)	$ (9,938)	$ 42,087	$ (6,425)	$ 47,200	$ 47,335
Income (loss) per share:					
Basic :					
Income (loss) from continuing operations	$ (0.34)	$ 1.51	$ (0.22)	$ 1.66	$ 1.74
Loss from discontinued operations	-	(0.08)	-	(0.06)	(0.13)
Net income (loss)	$ (0.34)	$ 1.43	$ (0.22)	$ 1.60	$ 1.61
Diluted:					
Income (loss) from continuing operations	$ (0.35)	$ 1.49	$ (0.22)	$ 1.66	$ 1.73
Loss from discontinued operations	-	(0.07)	-	(0.06)	(0.13)
Net income (loss)	$ (0.35)	$ 1.42	$ (0.22)	$ 1.60	$ 1.60
Weighted average number of ordinary shares used in computing basic net income (loss) per share (thousands)	29,523	29,415	29,532	29,416	29,437
Weighted average number of ordinary shares used in computing diluted net income (loss) per share (thousands)	29,523	29,543	29,532	29,538	29,550

* Includes revenues from related parties, in the amount of $3,506 and $ 3,967 for the six months ended June 30, 2006 and 2005, respectively, an amount of $1,762 and $2,144 for the three months ended June 30, 2006 and 2005, respectively, and an amount of $8,046 for the year ended December 31, 2005.

** Includes revenues from related parties in the amount of $143 for the six months ended June 30, 2005, an amount of $0 for the three months ended June 30, 2005, and an amount of $174 for the year ended December 31, 2005.

*** Reclassified due to discontinued operations.

The accompanying notes are an integral part of the consolidated financial statements.

STATEMENTS OF SHAREHOLDERS' EQUITY

U.S. dollars in thousands, except share and per share data

	Number of shares	Share capital	Additional paid-in capital	Accumulated other comprehensive income	Retained earnings	Total Shareholders' equity	Total comprehensive income (loss)
Balance as of January 1, 2005	29,414,424	$ 9,572	$ 270,005	$ 57,717	$ 51,786	$ 389,080	
Exercise of options	69,031	-	697			697	
Stock - based compensation	-	-	405	-	-	405	
Tax benefit in respect of options exercised	-	-	25	-	-	25	
Dividend paid					(88,450)	(88,450)	
Other comprehensive loss, net of tax:							
Unrealized loss on available for sale securities	-	-	-	(10,450)	-	(10,450)	$ (10,450)
Reclassification adjustment for gain realized and other than temporary impairment included in net income	-	-	-	(36,335)	-	(36,335)	(36,335)
Foreign currency translation adjustments	-	-	-	(191)		(191)	(191)
Net income	-	-	-	-	47,335	47,335	47,335
Balance as of December 31, 2005	29,483,455	$ 9,572	$ 271,132	$ 10,741	$ 10,671	302,116	
Total comprehensive income							$ 359
Unaudited							
Exercise of options	48,500	-	242	-	-	242	
Stock - based compensation	-	-	190	-	-	190	
Other comprehensive income (loss), net of tax:							
Unrealized loss on available for sale securities	-	-	-	(1,832)	-	(1,832)	$ (1,832)
Reclassification adjustment for loss realized and other than temporary impairment included in net loss	-	-	-	386	-	386	386
Foreign currency translation adjustments	-	-	-	258	-	258	258
Net loss	-	-	-	-	(9,938)	(9,938)	(9,938)
Balance as of June 30, 2006	29,531,955	$ 9,572	$ 271,564	$ 9,553	$ 733	$ 291,422	
Total comprehensive loss							$ (11,126)
Unaudited							
Balance as of January 1, 2005	29,414,424	$ 9,572	$ 270,005	$ 57,717	$ 51,786	$ 389,080	
Exercise of options	2,500	-	19	-	-	19	
Stock based compensation	-	-	163	-	-	163	
Other comprehensive loss, net of tax:							
Unrealized loss on available-for-sale securities	-	-	-	(13,252)	-	(13,252)	$ (13,252)
Reclassification adjustment for gain realized included in net income	-	-	-	(36,365)	-	(36,365)	(36,365)
Foreign currency translation adjustments	-	-	-	(163)	-	(163)	(163)
Net income	-	-	-	-	42,087	42,087	42,087
Balance as of June 30, 2005	29,416,924	$ 9,572	**$** 270,187	$ 7,937	$ 93,873	$ 381,569	
Total comprehensive loss							$ (7,693)

The accompanying notes are an integral part of the consolidated financial statements.

STATEMENTS OF SHAREHOLDERS' EQUITY

U.S. dollars in thousands, except share and per share data

	Number of shares	Share capital	Additional paid-in capital	Accumulated other comprehensive income	Retained earnings (Accumulated deficit)	Total Shareholders' equity	Total comprehensive income (loss)
Unaudited							
Balance as of April 1, 2006	29,531,955	$ 9,572	$ 271,468	$ 9,428	$ 7,158	$ 297,626	
Stock based compensation	-	-	96	-	-	96	
Other comprehensive income (loss), net of tax:							
Unrealized loss on available for sale securities	-	-	-	(352)	-	(352)	$ (352)
Reclassification adjustment for loss realized included in net loss and other than temporary impairment included in net loss	-	-	-	144	-	144	144
Foreign currency translation adjustments	-	-	-	333	-	333	333
Net loss	-	-	-	-	(6,425)	(6,425)	(6,425)
Balance as of June 30, 2006	29,531,955	$ 9,572	$ 271,564	$ 9,553	$ 733	$ 291,422	
Total comprehensive loss							$ (6,300)
Unaudited							
Balance as of April 1, 2005	29,414,424	$ 9,572	$ 270,114	$ 63,080	$ 46,673	$ 389,439	
Exercise of options	2,500	-	19	-	-	19	
Stock based compensation	-	-	54	-	-	54	
Other comprehensive loss, net of tax:							
Unrealized losses on available-for-sale securities	-	-	-	(18,586)	-	(18,586)	$ (18,586)
Reclassification adjustment for gain realized included in net income	-	-	-	(36,365)	-	(36,365)	(36,365)
Foreign currency translation adjustment	-	-	-	(192)	-	(192)	(192)
Net income	-	-	-	-	47,200	47,200	47,200
Balance as of June 30, 2005	29,416,924	$ 9,572	$ 270,187	$ 7,937	$ 93,873	$ 381,569	
Total comprehensive loss							$ (7,943)

The accompanying notes are an integral part of the consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

U.S. dollars in thousands

	Six months ended June 30, 2006	Six months ended June 30, 2005	Year ended December 31, 2005
	Unaudited	Unaudited	
Cash flows from operating activities			
Net income (loss)	$ (9,938)	$ 42,087	$ 47,335
Adjustments to reconcile net income to net cash used in operating activities:			
Equity in losses of affiliated companies	11,866	7,827	17,522
Minority interest in losses of subsidiaries	(7,037)	(645)	(5,160)
Loss (gain) from disposal of businesses and affiliated companies and changes in holdings in affiliated companies, net	7	(22,389)	(23,328)
Loss (gain) from sale of investments and other than temporary decline in available for sale securities	341	(56,423)	(56,515)
Gain from settlement of a subsidiary's loan	(2,708)	-	-
Gain from disposal of business included in discontinued operations	-	-	(213)
Depreciation and amortization	551	690	1,513
Impairment of intangible assets (discontinued operations)	-	1,329	1,329
Decline in value of other investments	-	636	636
Equity in losses (gains) of partnerships	618	60	(174)
Stock-based compensation and changes in liability in respect of call options	611	(1,128)	(811)
Deferred taxes, net	(35)	(4,645)	(7,288)
Changes in operating assets and liabilities			
Decrease (increase) in trade receivables	41	(278)	(947)
Decrease (increase) in other receivables and prepaid expenses	103	(112)	(38)
Decrease in trading securities, net	-	1	4
Decrease (increase) in inventories and contracts–in-progress	48	(400)	(519)
Increase (decrease) in trade payables	189	(1,028)	(834)
Increase (decrease) in other payables and accrued expenses	273	12,854	(12,139)
Other	731	(368)	(753)
Net cash used in operating activities	(4,339)	(21,932)	(40,380)
Cash flows from investing activities			
Investment in affiliated companies	(6,226)	(3,221)	(3,823)
Investment in other companies	(6,439)	(16,350)	(27,651)
Proceeds from sale of affiliated companies shares	992	10,076	10,522
Proceeds from repayment of loan granted to an affiliate company	-	2,253	2,253
Purchase of treasury stock from the minority by a subsidiary	-	(823)	(823)
Cash and cash equivalents resulting from newly consolidated subsidiaries (Sch. A)	-	-	-
Change in cash and cash equivalents resulting from disposal of business (Sch. B)	-	-	1,800
Proceeds from sale of available for sale securities	22,855	94,935	119,888
Proceeds from sale of other investments	-	93	237
Investments in deposits	(25,707)	(20,535)	(59,185)
Investment in available for sale securities	(24,668)	(18,405)	(35,405)
Proceeds from deposits	54,040	50,221	105,802
Purchase of property and equipment	(790)	(429)	(995)
Proceeds from sale of property and equipment	15	120	197
Net cash provided by investing activities	14,072	97,935	112,817
Cash flows from financing activities			
Proceeds from options exercised	242	19	697
Proceeds from exercise of options in a subsidiary	-	-	8
Repayment of long-term loans	(2)	(44)	(777)
Increase (decrease) in short-term bank loan, net	(400)	(76)	(1,079)
Receipt of short-term loans, convertible loans and long-term loans from minority shareholders of a subsidiary	2,197	500	1,003
Issuance of shares to the minority of a subsidiary	-	145	145
Issuance expenses in a subsidiary	-	(67)	(75)
Dividend paid	-	-	(88,450)
Net cash provided by (used in) financing activities	2,037	477	(88,528)
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	11,770	76,480	(16,091)
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF THE PERIOD	26,520	42,611	42,611
CASH AND CASH EQUIVALENTS AT THE END OF THE PERIOD	$ 38,290	$ 119,091	$ 26,520
LESS CASH AND CASH EQUIVALENTS ATTRIBUTED TO DISCONTINUED OPERATIONS	-	(291)	-
CASH AND CASH EQUIVALENTS AT THE END OF THE PERIOD	38,290	118,800	26,520

The accompanying notes are an integral part of the consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

U.S. dollars in thousands

	Six months ended June 30, 2006	Six months ended June 30, 2005	Year ended December 31, 2005
	Unaudited	Unaudited	
Supplemental cash flow information:			
Cash paid for:			
Income taxes	$ 672	$ 15,025	$ 30,591
Interest	$ 42	$ 109	$ 203
Proceeds from sale of an affiliate not yet received	$ -	$ 2,392	$ 1,958
Proceeds from sale of an affiliate received in Zoran shares	$ -	$ 7,700	$ 7,700

SCHEDULE A:

	Six months ended June 30, 2006	Six months ended June 30, 2005	Year ended December 31, 2005
Cash and cash equivalents resulting from newly consolidated subsidiaries			
Assets acquired and liabilities assumed at the purchase date:			
Working capital deficiency, net (except cash and cash equivalents)	$ -	$ -	$ 75
Property and equipment	-	-	(14)
Intangible assets	-	-	(237)
Accrued severance pay, net	-	-	27
Liability incurred	-	-	149
Cash and cash equivalents acquired	$ -	$ -	$ -

SCHEDULE B:

	Six months ended June 30, 2006	Six months ended June 30, 2005	Year ended December 31, 2005
Change in cash and cash equivalents resulting from disposal of businesses			
Assets and liabilities at date of sale:			
Working capital deficiency, net (except cash and cash equivalents)	$ -	$ -	$ (671)
Property and equipment	-	-	40
Intangible assets	-	-	2,389
Accrued severance pay, net	-	-	(171)
Gain resulting from sale of businesses	-	-	213
Net increase in cash and cash equivalents	$ -	$ -	$ 1,800

The accompanying notes are an integral part of the consolidated financial statements.

NOTE 1:- GENERAL

The accompanying unaudited condensed interim consolidated financial statements have been prepared as of June 30, 2006, and for the three and six months then ended in accordance with accounting principles generally accepted in the United States (U.S. GAAP) relating to the preparation of financial statements for interim periods. Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles in the United States but which are not required for interim reporting purposes, have been condensed or omitted. See Note 5 for the reconciliation from U.S. GAAP to accounting principles generally accepted in Israel ("Israeli GAAP").

These financial statements should be read in conjunction with the Company's annual financial statements and accompanying notes as of December 31, 2005, included in Form 20F for the year ended December 31, 2005 filed with the Securities and Exchange Commission ("the Company's annual financial statements").

The condensed interim consolidated financial statements reflect all adjustments which are, in the opinion of management considered, necessary to present fairly the financial position, results of operations and cash flows for the periods presented.

Results for the three and six months ended June 30, 2006 are not necessarily indicative of the results that may be expected for the year ending December 31, 2006.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES

a. The significant accounting policies followed in the preparation of these financial statements are identical to those applied in preparation of the latest annual financial statements, except as included in c below.

b. The financial statements have been prepared in U.S. dollars, since the functional currency of the Company and its principal subsidiaries is the U.S. dollar.

c. Effective January 1, 2006 ("the effective date") the Company applied SFAS No. 123(R), “Share-Base Payment”, which revises the previously effective SFAS No. 123 and supersedes APB No. 25. Generally, the approach in SFAS 123(R) is similar to the approach described in SFAS 123. However, SFAS 123(R) requires all share-based payments to employees, including grants of employee stock options, to be recognized in the income statement based on their fair values. Pro forma disclosure is no longer an alternative.

   The company, its subsidiaries and its affiliated companies adopted SFAS 123(R) using the modified-prospective method. According to the modified-prospective method, compensation cost is recognized beginning with the effective date (a) based on the grant date fair value estimated in accordance with the provisions of SFAS 123(R) for all share-based payments granted after the effective date and (b) based on the grant date fair value estimated in accordance with the provisions of SFAS 123 "Accounting for Stock-Based Compensation" ("SFAS 123") for all awards granted to employees prior to the effective date of SFAS 123(R) that remain unvested on the effective date.

   Previously, the Company and its subsidiaries adopted the fair-value-based method of accounting based on the provisions of SFAS 123 for share-based payments effective January 1, 2003 using the prospective methods described in SFAS 148 "Accounting for Stock- Based Compensation- Transition and Disclosure".

   Because 1) SFAS 123(R) must be applied not only to new awards but also to previously granted awards that are not fully vested on the effective date, 2) the Company adopted

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

c. (cont.)

SFAS 123 using the prospective transition method (which applied only to awards granted, modified or settled after January 1, 2003), and 3) prior to January 1, 2006, the Company's affiliated companies applied APB 25 whereby compensation cost measured based on the intrinsic value of the options granted, compensation cost for some previously granted awards in the Company, its subsidiaries and in its affiliated companies that were not previously recognized are recognized under SFAS 123(R).

As a result of adopting the provisions of SFAS 123(R) on January 1, 2006 by the Company, its subsidiaries and its affiliated companies, the Company recorded compensation expenses in the amount of approximately $700 and $1,100 during the three and six months periods ended June 30, 2006, respectively.

d. In July 2006, the FASB issued FASB Interpretation No. 48 "Accounting for Uncertainty in Income Taxes an Interpretation of FASB Statement No. 109" ("FIN 48"). FIN 48 clarifies the accounting for income taxes by prescribing the minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. FIN 48 utilizes a two-step approach for evaluating tax positions. Recognition (step one) occurs when an enterprise concludes that a tax position, based solely on its technical merits, is more-likely-than-not to be sustained upon examination. Measurement (step two) is only addressed if step one has been satisfied (i.e., the position is more-likely-than-not to be sustained). Under step two, the tax benefit is measured as the largest amount of benefit, determined on a cumulative probability basis that is more-likely-than-not to be realized upon ultimate settlement.

FIN 48 applies to all tax positions related to income taxes subject to the Financial Accounting Standard Board Statement No. 109, "Accounting for income taxes" ("FAS 109"). This includes tax positions considered to be "routine" as well as those with a high degree of uncertainty.

FIN 48 has expanded disclosure requirements, which include a tabular roll forward of the beginning and ending aggregate unrecognized tax benefits as well as specific detail related to tax uncertainties for which it is reasonably possible the amount of unrecognized tax benefit will significantly increase or decrease within twelve months. These disclosures are required at each annual reporting period unless a significant change occurs in an interim period.

FIN 48 is effective for fiscal years beginning after December 15, 2006. The cumulative effect of applying FIN 48 will be reported as an adjustment to the opening balance of retained earnings.

The Company is currently evaluating the effect of the adoption of FIN 48 on its financial statements.

NOTE 3:- MAJOR TRANSACTIONS

a. **Partner Communications Company Ltd. ("Partner")**

On March 21, 2006, Elron completed the acquisition of approximately 823,000 shares of Partner from one of the other Israeli founding shareholders of Partner for approximately $5,300, reflecting approximately 15% discount from the market price at the date of the agreement. Upon completion of the acquisition, Elron holds approximately 2.6% of Partner.

Almost all of Partner shares held by the Company are subject to certain transfer restrictions under Partner's Israeli Communications license. The shares are accounted for as available-for-sale securities.

b. **Nulens**

As described in Note 8 (c) to the Company's annual financial statements, on April 21, 2005, Elron completed an investment of approximately $2,900 in Nulens Ltd. ("Nulens"), in consideration for 763,584 Series A preferred shares, as part of an aggregate investment of approximately $3,400. Elron's investment was in two installments, the first of approximately $1,700 was invested immediately for approximately 17% of Nulens on a fully diluted and on an as converted basis and an additional amount of approximately $1,100 was invested on March 9, 2006. Simultaneously with the $1,100 investment, Elron invested an additional amount of $1,500in 241,158 Series B preferred shares. The investment in preferred B shares was part of a new round of investment in the aggregate amount of approximately $6,000. The new round was led by Warburg Pincus, a leading global private equity fund. Following the above investments, Elron holds 25% of Nulens, on a fully diluted and on an as converted basis. Nulens is an Israeli medical devices company operating in the field of intra-ocular lenses mainly for cataract and presbyopia procedures.

Since the investments in preferred A and B shares are not considered to be investments that are in-substance-common stock, the investment in Nulens is accounted for under the cost method.

c. **Safend**

On January 2, 2006, Elron completed an investment of approximately $3,700 in Safend Ltd. ("Safend"), in consideration for 1,942,261 Series B preferred shares, as part of an aggregate investment of approximately $7,400. Following Elron's investment, Elron holds approximately 22% of Safend on a fully diluted and on an as converted basis. Safend is an Israeli company which develops comprehensive desktops and laptops endpoint security solutions.

Since the investment in preferred B shares is not considered to be an investment that is in-substance-common stock, the investment in Safend is accounted for under the cost method.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
U.S. dollars in thousands, except share and per share data

NOTE 3:- MAJOR TRANSACTIONS (Cont.)

d. **Mediagate**

In February 2006, Mediagate's bank loan in the amount of approximately $2,800 was settled in consideration for $100. As a result, according to the provisions of FAS 140 "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities" Elron recorded in the first quarter of 2006 a gain of approximately $2,700 which is included in other income in the statements of operations.

e **AMT**

On June 8, 2006, Elron completed an investment of $5,000 in convertible A1 notes of Advanced Metal Technology Ltd. (AMT), as part of a financing round of $14,000 led by Shamrock Israel Growth Fund, an Israeli private equity fund. The investment in AMT was in two installments, the first of $2,500 was invested immediately, and the additional $2,500 investment is subject to certain conditions. In addition, Elron and other shareholders of AMT converted previously granted loans in the amount of $1,000 into convertible A1 notes of AMT, of which Elron's share is $500. Following the above investment, Elron's holdings in AMT decreased from approximately 42% to 34% on an as converted basis. The decrease in holdings had no effect on the results of operations**.**

f. **GIVEN**

Subsequent to the balance sheet date, Elron has purchased, in a series of open market transactions, approximately 540,000 ordinary shares of Given Imaging Ltd. ("Given"), for an aggregate purchase consideration of approximately $10,000. As a result of the transactions, Elron's direct and indirect ownership interest in Given (through its direct holdings and its holdings in its subsidiary, RDC-Rafael Development Corporation Ltd.) increased from approximately 19.3% to approximately 21.2% of Given outstanding ordinary shares. In parallel transactions, DIC purchased the same number of shares of Given for the same aggregate consideration, increasing its holding in Given from approximately 12.4% to approximately 14.3% of Given's outstanding ordinary shares.

g. **ONCURA**

In light of Oncura's results, the Company recorded in the second quarter of 2006 an impairment loss on the investment in Oncura in the amount of $6.1 ($2.5 net of minority interest), due to an other than temporary decline in value of such investment. The impairment loss was presented in the statement of operations in the line item "equity in losses of affiliated companies".

NOTE 4:- CONTINGENT LIABILITIES

There were no material changes in the status of the Company’s contingent liabilities as described in the Company's annual financial statements, the details of which are as follows:

1. During September 1999, the Company received copies of two claims and a request to approve such claims as a class action on behalf of public shareholders of Elscint (formerly an affiliated company) against the Company and others. The allegation raised by the claimants related to the decision regarding the sale of Elscint’s substantial assets. The claim has been stayed pursuant to an arrangement reached by the parties pending the outcome of the appeal in the claim described in paragraph 2 below. The arrangement

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
U.S. dollars in thousands, except share and per share data

NOTE 4:- CONTINGENT LIABILITIES (Cont.)

provides that if the appeal as described in paragraph 2 below is accepted, then the proceedings to recognize the lawsuit as a class action will proceed. Otherwise, the application to recognize the claim as a class action suit will be dismissed.

2. On November 2, 1999, the Company received a copy of a claim, and a request to approve such a claim, as a class action on behalf of some institutional investors and others and those who held shares in Elscint on September 6, 1999. The allegations raised against the

Company and certain of its officers including former officers, among others, relate to the period prior to the sale of the Company's holdings in Elbit Medical Imaging ("EMI") (the parent company of Elscint and formerly an affiliated company). The claimants seek a court order pursuant to which EMI would be compelled to execute the alleged buy-out of Elscint's share at $14 per share or other remedies. On August 16, 2000, the Haifa District court dismissed the application to recognize the claim as a class action. Some of the claimants applied for and have been granted permission to appeal to the Supreme Court in Israel, which appeal is currently pending.

In addition, in February 2001, the claimants submitted a revised claim similar to the previous one but not as a class action. It has not been determined when the defendants are required to file their statements of defense to the claim. The claimants and the defendants are currently involved in various proceedings, mostly regarding the disagreement concerning the court fees.

The Company denies all the allegations set forth in the above claims, and based on legal advice received, management is of the opinion that the Company has good defense arguments which, if accepted, will cause dismissal of the above allegations.

NOTE 5:- RECONCILIATION TO ISRAELI GAAP

The consolidated financial statements of the Company have been prepared in accordance with U.S. GAAP. Had the consolidated financial statements been prepared in accordance with Israeli GAAP, the effects on the financial statements would have been as follows:

a. Effect on the statement of operations:

	Six months ended June 30, 2006		
	As reported	Adjustments	As per Israeli GAAP
		Unaudited	
Net loss	$ (9,938)	$ (8,027)	$ (17,965)
Basic net loss per share	(0.34)	(0.27)	(0.61)
Diluted net loss per share	(0.35)	(0.27)	(0.62)

	Six months ended June 30, 2005		
	As reported	Adjustments	As per Israeli GAAP
		Unaudited	
Net income	$ 42,087	$ 18,217	$ 60,304
Basic net loss per share	1.43	0.62	2.05
Diluted net loss per share	1.42	0.62	2.04

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
U.S. dollars in thousands, except share and per share data

NOTE 5:- RECONCILIATION TO ISRAELI GAAP (Cont.)

a. Effect on the statement of operations: (Cont.)

	Three months ended June 30, 2006		
	As reported	Adjustments	As per Israeli GAAP
		Unaudited	
Net loss	$ (6,425)	$ (3,345)	$ (9,770)
Basic net loss per share	(0.22)	(0.11)	(0.33)
Diluted net loss per share	(0.22)	(0.11)	(0.33)

	Three months ended June 30, 2005		
	As reported	Adjustments	As per Israeli GAAP
		Unaudited	
Net income	$ 47,200	$ 20,789	$ 67,989
Basic net loss per share	1.60	0.71	2.31
Diluted net loss per share	1.60	0.71	2.31

	Year ended December 31, 2005		
	As reported	Adjustments	As per Israeli GAAP
		Audited	
Net income	$ 47,335	$ 7,147	$ 54,482
Basic net income per share	1.61	0.24	1.85
Diluted net income per share	1.60	0.24	1.84

b. Effect on the balance sheet:

	June 30, 2006		
	As reported	Adjustments	As per Israeli GAAP
		Unaudited	
Total assets	$ 335,811	$ (77,368)	$ 258,443
Total liabilities including minority interest	44,389	(16,573)	27,816
Total equity	291,422	(60,795)	230,627

	December 31, 2005		
	As reported	Adjustments	As per Israeli GAAP
		Audited	
Total assets	$ 353,773	$ (75,361)	$ 278,412
Total liabilities including minority interest	51,657	(21,145)	30,512
Total equity	302,116	(54,216)	247,900

c. Material adjustments:

The abovementioned adjustments result primarily from the differences between U.S. GAAP and Israeli GAAP detailed in Note 26 to the Company's annual financial statements for 2005.

ANNEX TO THE CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

Details relating to major investments as of June 30, 2006:

	% of ownership interest (1)	Carrying value of the investment as of June 30, 2006 (2)	Market value of the publicly traded investments as of: June 30, 2006	August 9, 2006
Consolidated Companies:				
Galil Medical Ltd. (3)	40%	1,771	-	-
3DV Systems Ltd. (3)	62%	(225)	-	-
Starling (3)	50%	476	-	-
SELA (3)	39%	916	-	-
Enure (formerly: Gaia)	57%	2,109	-	-
Mendingo (3)	50%	5	-	-
Affiliated Companies (equity):				
Given Imaging Ltd. (Nasdaq: GIVN) (3) (5)	19%	61,611	82,930	107,990
NetVision Ltd. (TASE: NTSN)	39%	8,118	39,476	39,554
ChipX	29%	3,789	-	-
CellAct Ltd.	45%	468	-	-
Oncura (4)	10%	6,016	-	-
AMT	34%	3,151	-	-
Wavion, Inc.	38%	1,095	-	-
Pulsicom Israel Technologies Ltd.	18%	1	-	-
Notal Vision, Inc.	23%	-	-	-
Available for sale:				
Partner (Nasdaq: PTNR)	3%	29,569	32,140	35,741
EVS (Nasdaq: EVSNF.OB)	9%	1,215	1,509	1,509
Partnership:				
Gemini Israel Fund L.P.	5%	33	-	-
InnoMed Ventures L.P.	14%	3,347	-	-
Cost:				
Jordan Valley	28%	8,137	-	-
Impliant	22%	8,340	-	-
Teledata Ltd.	21%	16,000	-	-
Nulens Ltd.	29%	4,360	-	-
Brainsgate Ltd.	22%	6,947	-	-
Safend Ltd.	26%	3,700	-	-

(1) On the basis of the outstanding share capital.

(2) Includes loans and convertible notes.

(3) Represents the carrying value and the ownership interest of the investment in Elron's books and Elron's share in the carrying value and ownership interest of the investment in RDC's books.

(4) Represents Elron's share in the carrying value and the ownership interest of the investment in Galil's books.

(5) During August 2006 Elron purchased 539,721 ordinary shares of Given in consideration for approximately $10,000 and as a result Elron's % of ownership interest was increased from 19.3% to 21.2%.

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