ELRON ELECTRONIC INDUSTRIES LTD.

AND ITS SUBSIDIARIES

CONDENSED INTERIM CONSOLIDATED

FINANCIAL STATEMENTS

As of March 31, 2003

(Unaudited)

ELRON ELECTRONIC INDUSTRIES LTD.

AND ITS SUBSIDIARIES

CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

As of March 31, 2003

(Unaudited)

C O N T E N T S

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ELRON ELECTRONIC INDUSTRIES LTD.
AND ITS SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

In thousands of U.S. Dollars ,except share data

	March 31, 2003 (Unaudited)	December 31, 2002 (Audited)
ASSETS		
Current assets:		
Cash and cash equivalents	$ 59,472	$ 67,901
Marketable securities	2,403	3,180
Trade receivables, net	6,489	9,238
Other receivables and prepaid expenses	5,183	4,528
Inventories and contracts-in-progress	2,581	2,197
Total current assets	76,128	87,044
Long-term assets:		
Investments in affiliated companies	132,080	131,256
Investments in other companies and long-term receivables	90,544	97,158
Long-term debentures and deposits	30,129	28,928
Deferred taxes	3,491	2,990
Severance pay deposits	2,358	2,262
Total long-term assets	258,602	262,594
Property and equipment, net	11,462	11,576
Other assets:		
Goodwill	21,538	21,538
Other intangible assets	18,101	18,577
	39,639	40,115
Total assets	$ 385,831	$ 401,329

The accompanying notes to the consolidated financial statements form an integral part thereof.

ELRON ELECTRONIC INDUSTRIES LTD.
AND ITS SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

In thousands of U.S. Dollars ,except share data

	March 31, 2003 (Unaudited)	December 31, 2002 (Audited)
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Short-term loans from banks	$ 13,968	$ 15,362
Current maturities of long-term loans from banks and others	17,488	17,637
Trade payables	4,164	5,738
Other payables and accrued expenses	15,361	16,516
Total current liabilities	50,981	55,253
Long-term liabilities:		
Long-term loans from banks and others	50,180	49,389
Accrued severance pay and retirement obligations	3,083	2,921
Deferred taxes	22,391	23,650
Other	552	414
Total long-term liabilities	76,206	76,374
Minority interest	3,279	3,185
Shareholders' equity:		
Ordinary shares of NIS 0.003 par value; Authorized – 35,000,000 shares as of March 31,2003 and December 31, 2002 respectively; Issued and outstanding - 29,180,970 shares as of March 31, 2003 and December 31, 2002, respectively;	9,572	9,572
Additional paid-in capital	267,817	267,482
Accumulated other comprehensive income	4,653	7,529
Accumulated deficit	(26,677)	(18,066)
Total shareholders' equity	255,365	266,517
Total liabilities and shareholders' equity	$ 385,831	$ 401,329

The accompanying notes to the consolidated financial statements form an integral part thereof.

ELRON ELECTRONIC INDUSTRIES LTD.

AND ITS SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

In thousands of U.S. Dollars, except share and per share data

	For the three months ended March 31, 2003	For the three months ended March 31, 2002(*)	For the year ended December 31, 2002
	(Unaudited)	(Unaudited)	(Audited)
Income			
Net revenues	$ 5,591	$ 5,906	$ 23,468
Equity in losses of affiliated companies	(2,295)	(5,678)	(21,911)
Gain from disposal and changes in holdings in subsidiaries and affiliated companies, net	371	140	6,888
Other income (expenses), net	(1,223)	488	(743)
	2,444	856	7,702
Costs and Expenses			
Cost of revenues	2,480	3,020	11,557
Research and development costs, net	2,089	1,921	7,818
Marketing and selling expenses, net	5,134	2,439	14,428
General and administrative expenses	3,272	2,361	11,272
Restructuring costs	-	22	2,318
Amortization of intangible assets	549	435	2,058
Financial expenses (income), net	320	(230)	474
	13,844	9,968	49,925
Loss before taxes on income	(11,400)	(9,112)	(42,223)
Tax benefit	363	733	2,855
Loss from continuing operations after taxes on income	(11,037)	(8,379)	(39,368)
Minority interest in losses of subsidiaries	1,972	118	2,823
Loss from continuing operations	(9,065)	(8,261)	(36,545)
Gain (loss) from discontinued operations	454	-	(2,756)
Net loss	$ (8,611)	$ (8,261)	$ (39,301)
Loss per share:			
Basic and diluted loss per share data -			
Loss from continuing operations	$ (0.31)	$ (0.39)	$ (1.39)
Gain (loss) from discontinued operations	0.01	-	(0.11)
Net loss	$ (0.30)	$ (0.39)	$ (1.50)
Weighted average number of ordinary shares used in computing basic and diluted loss per share (thousands)	29,181	21,214	26,272

(*) Restated – See Note 3(D).

The accompanying notes to the consolidated financial statements form an integral part thereof.

ELRON ELECTRONIC INDUSTRIES LTD.
AND ITS SUBSIDIARIES

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

In thousands of U.S. Dollars , except share and per share data

	Number of shares	Share capital	Additional paid-in capital	Accumulated other comprehensive income	Accumulated deficit	Total shareholders' equity	Total comprehensive loss
Audited							
Balance as of January 1, 2002 (*)	21,213,664	$ 9,567	$165,680	$42,231	$21,235	$238,713	
Exercise of options	87,863	-	605			605	
Issuance of shares pursuant the merger with Elbit	5,617,601	4	71,191	-	-	71,195	
Issuance of shares pursuant the purchase of DEP	2,261,843	1	29,448	-	-	29,449	
Changes in additional paid-in capital in affiliated companies	-	-	336	-	-	336	
Amortization of deferred stock compensation	-	-	222	-	-	222	
Other comprehensive loss, net of tax:							
Unrealized losses on available for sale marketable securities	-	-	-	(33,035)	-	(33,035)	(33,035)
Reclassification adjustment for gain realized net of other than temporary decline included in net loss	-	-	-	(1,070)	-	(1,070)	(1,070)
Minimum pension liability in an affiliated Company	-	-	-	(597)	-	(597)	(597)
Net loss	-	-	-	-	(39,301)	(39,301)	(39,301)
Balance as of December 31, 2002	29,180,971	$ 9,572	$267,482	$ 7,529	$ (18,066)	$ 266,517	
Total comprehensive loss							$ (74,003)
Unaudited							
Other comprehensive income, net of tax:							
Unrealized losses on available for sale marketable securities	-	-	-	(2,805)	-	(2,805)	(2,805)
Reclassification adjustment for gain realized included in net loss	-	-	-	(18)	-	(18)	(18)
Foreign currency translation adjustment	-	-	-	(53)	-	(53)	(53)
Changes in additional paid-in capital in affiliated companies	-	-	277	-	-	277	-
Amortization of deferred stock compensation	-	-	58	-	-	58	-
Net loss	-	-	-	-	(8,611)	(8,611)	(8,611)
Balance as of March 31, 2003	29,180,971	$ 9,572	$ 267,817	$ 4,653	$ (26,677)	$ 255,365	
Total comprehensive loss							$ (11,487)
Unaudited							
Balance as of January 1, 2002 (*)	21,213,664	$ 9,567	$ 165,680	$ 42,231	$ 21,235	$ 238,713	
Other comprehensive income, net of tax:							
Unrealized losses on available for sale marketable securities	-	-	-	(12,127)	-	(12,127)	(12,127)
Reclassification adjustment for gain realized included in net loss	-	-	-	(1,331)	-	(1,331)	(1,331)
Foreign currency translation adjustment	-	-	-	10	-	10	10
Changes in additional paid-in capital in affiliated companies	-	-	11	-	-	11	-
Amortization of deferred stock compensation	-	-	56	-	-	56	-
Net loss	-	-	-	-	(8,261)	(8,261)	(8,261)
Balance as of March 31, 2002 (*)	21,213,664	$ 9,567	$ 165,747	$ 28,783	$ 12,974	$ 217,071	
Total comprehensive loss							$ (21,709)

(*) Restated – See Note 3(D).

The accompanying notes to the consolidated financial statements form an integral part thereof.

ELRON ELECTRONIC INDUSTRIES LTD.

AND ITS SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

In thousands of U.S. Dollars , except share and per share data

	For the three months ended March 31, 2003 (Unaudited)	For the three months ended March 31, 2002 (*) (Unaudited)	For the year ended December 31, 2002 (Audited)
CASH FLOWS FROM OPERATING ACTIVITIES			
Net loss	$ (8,611)	$ (8,261)	$ (39,301)
Adjustments to reconcile net loss to net cash used in operating activities:			
Equity in losses of affiliated companies	2,295	5,678	21,911
Dividend from affiliated companies	-	-	2,670
Minority's interest in losses of subsidiaries	(1,972)	(118)	(2,823)
Gain from disposal and changes in holdings in affiliated companies, net	(371)	(140)	(6,888)
Gain (loss) from sale of investments in available for sale securities	28	(605)	(706)
Gain resulting from sale of business	-	-	(1,991)
Depreciation and amortization	1,084	834	4,372
Decline in value of other investments and accrued interest	1,238	(3)	2,481
Amortization of deferred stock compensation and call options	187	223	(104)
Deferred taxes, net	(412)	(718)	(3,398)
Decrease in trade receivables	2,749	300	2,515
Decrease (increase) in other accounts receivable and prepaid expenses	(652)	852	3,439
Decrease (increase) in trading marketable securities, net	(6)	182	231
Decrease (increase) in inventories and contracts–in-progress	(717)	55	698
Decrease in trade payables	(1,574)	(1,149)	(1,385)
Decrease in other accounts payable and accrued expenses	(1,133)	(100)	(11,314)
Other	367	(253)	383
Net cash used in operating activities	(7,500)	(3,223)	(29,210)
CASH FLOWS FROM INVESTING ACTIVITIES			
Investment in affiliated companies	(3,174)	(2,006)	(19,951)
Proceeds from sale of Elbit Systems shares	-	-	5,862
Proceeds from sale of Given Imaging shares	813	-	6,918
Cash and cash equivalents resulting from the merger with Elbit (Schedule A)	-	-	14,883
Cash and cash equivalents resulting from the share purchase of DEP (Schedule B)	-	-	284
Cash and cash equivalents resulting from newly consolidated subsidiaries (Mediagate and Galil Medical) (Schedule C)	-	-	2,978
Cash and cash equivalents resulting from sale of businesses and subsidiaries (Schedule D)	-	-	(1,984)
Investment in other companies	(600)	(1,100)	(3,700)
Proceeds from sale of investments in other companies	-	-	405
Proceeds from sale of available for sale securities	2,614	789	890
Investments in deposits	(2,346)	(2,853)	(11,381)
Proceeds from maturities of held to maturity debentures and from deposits	1,209	1,100	4,482
Purchase of property and equipment	(241)	(204)	(969)
Proceeds from sale of property and equipment	106	33	515
Proceeds from sale of certain activities	-	3,816	6,589
Net cash provided by (used in) investing activities	(1,619)	(425)	5,821
CASH FLOWS FROM FINANCING ACTIVITIES			
Proceeds from exercise of options	-	-	605
Proceeds from exercise of options in a subsidiary	-	-	2
Long-term loans from banks	1,201	1,860	9,152
Repayment of loans from shareholder	-	-	(1,378)
Repayment of long-term loans	(82)	(291)	(706)
Decrease in short-term bank credit, net	(1,554)	(1,816)	(8,954)
Proceeds from issuance of notes to the minority in a subsidiary	1,125	-	2,165
Net cash provided by (used in) financing activities	690	(247)	886
DECREASE IN CASH AND CASH EQUIVALENTS	(8,429)	(3,895)	(22,503)
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF THE PERIOD	67,901	90,404	90,404
CASH AND CASH EQUIVALENTS AT THE END OF THE PERIOD	$ 59,472	$ 86,509	$ 67,901

(*) Restated – See Note 3(D).

The accompanying notes to the consolidated financial statements form an integral part thereof.

ELRON ELECTRONIC INDUSTRIES LTD.
AND ITS SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS (Cont.)

In thousands of U.S. Dollars, except share and per share data

	For the three months ended March 31, 2003 (Unaudited)	For the three months ended March 31, 2002 (Unaudited)	For the year ended December 31, 2002 (Audited)
Supplemental cash flow information:			
Cash paid for:			
Income taxes	$ 18	$ 349	$ 521
Interest	$ 419	$ 338	$ 1,916
Non-cash transaction:			
Receivable on account of activity sale	$ -	$ 2,795	$ -
Warrant in a subsidiary granted to bank in respect of credit line	$ 459	$ -	$ -

SCHEDULE A:

Cash and cash equivalents resulting from the merger with Elbit

	Year ended December 31, 2002 (Audited)
Assets acquired and liabilities assumed on the merger date:	
Working capital (except cash and cash equivalents)	$ 6,970
Property and equipment	(9,225)
Investments in affiliated companies	(5,423)
Other investments	(111,482)
Other long-term assets	(1,820)
Goodwill	(18,275)
Long-term liabilities	40,123
Investment at equity prior to merger	42,739
Minority interests	82
Issuance of shares	71,194
Cash and cash equivalents acquired	$ 14,883

SCHEDULE B:

Cash and cash equivalents resulting from the share purchase of DEP

	Year ended December 31, 2002 (Audited)
Assets acquired and liabilities assumed at the share	
Working capital (except cash and cash equivalents)	$ 19,115
Property and equipment	(28)
Investments in affiliated companies	(40,493)
Other investments	(3,315)
Other assets	(5,486)
Long-term liabilities	1,451
Investment at equity prior to acquisition	385
Minority interests	(794)
Issuance of shares	29,449
Cash and cash equivalents acquired	$ 284

The accompanying notes to the consolidated financial statements form an integral part thereof.

ELRON ELECTRONIC INDUSTRIES LTD.

AND ITS SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS (Cont.)

In thousands of U.S. Dollars

SCHEDULE C:

	Year ended December 31, 2002 (Audited)
Cash and cash equivalents resulting from newly consolidated subsidiaries	
Assets acquired and liabilities assumed at the purchase date:	
Working capital (except cash and cash equivalents)	$ 3,230
Property and equipment	(2,007)
Other assets	(12,024)
Deferred taxes	3,260
Accrued severance pay, net	179
Investment at equity prior to acquisition	8,231
Minority interests	2,109
Cash and cash equivalents acquired	$ 2,978

SCHEDULE D:

	Year ended December 31, 2002 (Audited)
Cash and cash equivalents resulting from sale of business and subsidiaries	
Assets and liabilities at date of sale:	
Working capital (except cash and cash equivalents)	$ (677)
Property and equipment	266
Other assets	200
Accrued severance pay, net	(33)
Gain resulting from sale of business	1,991
Marketable securities received	(1,600)
Other investments received	(2,131)
Cash and cash equivalents received	$ (1,984)

The accompanying notes to the consolidated financial statements form an integral part thereof.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

In thousands of U.S. Dollars
(Unaudited)

Note 1 - GENERAL

The accompanying unaudited condensed interim consolidated financial statements have been prepared as of March 31, 2003, and for the three 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. See Note 8 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, 2002.

Comparative data in the condensed interim consolidated financial statements for the three months ended March 31, 2002 have been restated - see Note 3D.

The condensed interim consolidated financial statements reflect all adjustments which are, in the opinion of management, necessary to present fairly the financial position and the results of operations and cash flows for the period presented. All such adjustments were of a normal recurring nature.

Results for the three month period ended March 31, 2003 are not necessarily indicative of the results that may be expected for the year ending December 31, 2003.

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.

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.

B. RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In January 2003, the Financial Accounting Standards Board issued Interpretation No. 46, *Consolidation of Variable Interest Entities, an interpretation of Accounting Research Bulletin No. 51* ("the interpretation"). In general, a variable interest entity (VIE) is an entity that has (1) insufficient amount of equity for the entity to carry on its principal operations, without additional subordinated financial support from other parties, (2) a group of equity investors that do not have the ability through voting or similar rights to make decisions about the entity's activities, or (3) a group of equity investors that do not have the obligation to absorb the entity's losses or have the right to receive the benefits of the entity. The interpretation requires the consolidation of a VIE by the primary beneficiary. The primary beneficiary is the entity that absorbs a majority of the entity's expected losses, receives a majority of the entity's expected residual returns, or both, as a result of ownership, contractual or other financial interests in the entity.

Note 2 - SIGNIFICANT ACCOUNTING POLICIES (Cont.)

B. RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS (Cont.)

Presently, entities are generally consolidated by an enterprise that has a controlling financial interest through ownership of a majority voting interest in the entity.

The provisions of this interpretation are to be applied commencing from July 1, 2003, to variable interests in VIEs created before February 1, 2003 and immediately to variable interests in VIEs created after January 31, 2003. Since the company has no such interests in VIEs created after January 31, 2003, the application of this interpretation had no impact on the Company's consolidated results of operations or consolidated balance sheet to date.

The Company has investments in and loans to various companies that are engaged primarily in the fields of high technology. Most of these companies are in their early stages of development and will require substantial third party investments until they can finance their activities without additional support from other parties. These companies are currently primarily funded with financing from venture capital funds, other holding companies and private investors. The investments in these companies are consolidated or accounted for by the equity or cost method by the Company.

The Company is currently evaluating the effects of this interpretation in respect of its investments. It is likely that some of its investees may be considered a VIE in accordance with the interpretation. Accordingly, if it is determined that the Company is the primary beneficiary of a VIE, the Company will be required to consolidate the financial statements of such a VIE with its own financial statements commencing from July 1, 2003.

The Company's maximum exposure to loss as of March 31, 2003, does not exceed its investment in any of these companies.

Note 3 - MAJOR TRANSACTIONS

A. GALIL MEDICAL LTD. ("Galil")

1. In the first quarter of 2003, Elron invested approximately $1,900 in Galil in the form of notes convertible into Galil's shares ("Notes") pursuant to addenda to the note purchase agreement which Galil originally signed with certain existing shareholders, including Elron, in May 2002 (the "Note Agreement"), upon the same terms and conditions as the Note Agreement.

   Subsequent to the balance sheet date, during April 2003, Elron and RDC signed an additional addendum to the Note Agreement according to which Elron invested $600 and RDC invested $840 in the form of Notes upon the same terms and conditions as the Note Agreement.

Note 3 - MAJOR TRANSACTIONS (Cont.)

A. GALIL MEDICAL LTD ("Galil") (Cont.)

2. Subsequent to the balance sheet date, on April 22, 2003, Galil announced the signing of a definitive agreement with Amersham (LSE, NYSE, OSE: AHM) ("Amersham") to merge Amersham Health's brachytherapy business with Galil's urology business. The new company will provide minimally invasive treatment options for prostate cancer using brachytherapy and cryotherapy technology.

According to the agreement, at the closing, Amersham will hold 78% and Galil will hold 22% of the new company. In exchange for Galil's shares and Amersham's shares in the new company, Galil and Amersham will contribute the assets necessary for the new company to conduct the Cryo business and the brachytherapy business respectively in the urology field. In addition, at the closing, Galil shall purchase 3% of the new company from Amersham in consideration for $4,500 in cash, resulting in an aggregate ownership interest of 25% upon the completion of the transaction. The transaction is subject to regulatory approvals and is expected to close by the end of July 2003.

B. NOTAL VISION LTD. ("Notal")

In October 2002, Elron signed an agreement to invest $2,000 in Notal Vision Ltd. ("Notal"), out of an aggregate amount of $4,000 raised by Notal. Notal, an Israeli medical device company, operates in the field of early detection of Age Related Macular Deterioration (AMD). The investment was completed in January 2003. As a result of the investment, Elron holds 25% of Notal's outstanding shares.

The excess of the purchase price over the equity acquired, in the amount of approximately $1,000, was assigned to technology and to a distribution agreement, which will be amortized over a period of up to 7 years.

C. GIVEN IMAGING LTD. ("Given")

Subsequent to the balance sheet date on May 12, 2003, a Share Purchase Agreement ("the SPA") was signed between RDC, Elron and Rafael Armament Development Authority Ltd. ("Rafael"). According to the SPA, RDC sold two million unregistered shares of Given to Elron and Rafael (one million each) for a total consideration of $12,184. RDC used $4.0 million of the proceeds to repay shareholders' loans to each of Rafael and Elron. As a result of the above sale, there will be no change in Elron's direct and indirect holdings in Given. Accordingly, the above sale will not have any effect on the Company's consolidated results of operations.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

In thousands of U.S. Dollars
(Unaudited)

Note 3 - MAJOR TRANSACTIONS (Cont.)

D. RESTATEMENT

Elron has direct holdings in certain companies in which RDC also holds shares. As a result of the purchase of DEP in May 6, 2002 (See Note 3B(1) to the company's annual financial statements for the year ended December 31, 2002), Elron's aggregate interest in these companies has increased and enabled Elron to exercise significant influence in these companies. In accordance with U.S. Accounting Principles Board Opinion No. 18, "The Equity Method of Accounting for Investments in Common Stock", Elron's direct holdings in these companies, which had been accounted for by Elron at cost or as available for sale securities, were accounted for retroactively under the equity method of accounting ("step-by-step acquisition"). Implementing step-by-step acquisition resulted in a restatement of Elron's financial statements for all prior periods in which Elron's investments in these companies had been recorded at cost or as available for sale securities.

Following are the effects of the restatement:

1) Consolidated statements of operations

	For the three months ended March 31, 2002		
	As reported	Effect of restatement	As restated
Equity in losses of affiliated companies	(4,960)	(718)	(5,678)
Net loss	(7,543)	(718)	(8,261)
Basic and diluted net loss per share	(0.36)	(0.03)	(0.39)

2) Total Comprehensive loss

	For the three months ended March 31, 2002		
	As reported	Effect of restatement	As restated
Total Comprehensive loss	(22,932)	1,223	(21,709)

In thousands of U.S. Dollars

Note 4 - SUPPLEMENTAL PRO FORMA INFORMATION (UNAUDITED)

A. The pro forma information for 2002 presents the results of operations of Elron after giving effect to the merger with Elbit, the share purchase of DEP and the acquisition of a controlling interest in Galil and MediaGate (all above transactions are detailed in Note 3A(3), 3B(1), 3D(2), 3F(2), respectively, to the company's annual financial statements for the year ended December 31, 2002) as if they had been in effect at January 1, 2002, and includes the effect of amortization of identifiable intangible assets from that date.

B. The following pro forma information is based upon the historical financial statements of Elron (after restatement, as discussed in Note 3D) and upon the historical financial statements of Elbit (after reclassification of discontinuing operations), DEP, Galil and MediaGate. The pro forma data does not incorporate, nor does it assume, any benefits from cost savings or synergies of the combined companies.

C. The pro forma data is presented for comparative purposes only and is not necessarily indicative of the operating results that would have occurred had the merger with Elbit, the share purchase of DEP or the acquisition of a controlling interest in Galil and MediaGate been consummated at the date indicated, nor are they necessarily indicative of future operating results or financial condition.

PRO FORMA COMBINED RESULTS OF OPERATIONS

	For the three months ended March 31, 2003 As reported	For the three months ended March 31, 2002 (*)Pro Forma	For the year ended December 31, 2002 Pro Forma
Net revenues	$ 5,591	$ 6,936	$ 25,897
Equity in losses of affiliated companies	(2,295)	(3,068)	(14,030)
Gain (loss) from disposal and changes in holdings in subsidiaries and affiliated companies, net	371	(74)	6,674
Other Income (expenses), net	(1,223)	(434)	1,801
Total income	2,444	3,360	20,342
Costs and expenses	13,844	17,678	69,822
Loss before tax benefit and minority interests	$ (11,400)	$ (14,318)	$ (49,480)
Loss from continuing operations	$ (9,065)	$ (11,794)	$ (40,294)
Net loss	$ (8,611)	$ (17,773)	$ (52,371)
Basic and diluted loss from continuing operations per share	$ (0.31)	$ (0.40)	$ (1.38)
Basic and diluted net loss per share	$ (0.30)	$ (0.61)	$ (1.80)
Weighted average number of ordinary shares used in computation of basic and diluted loss per share (thousands)	$ 29,181	$ 29,093	$ 29,131

(*) Restated – See Note 3(D).

In thousands of U.S. Dollars

Note 5 - STOCK BASED EMPLOYEE COMPENSATION

The Company has elected to follow Accounting Principles Board Opinion No. 25, ("APB 25") "Accounting for Stock Issued to Employees" and the FASB Interpretation No. 44, "Accounting for Certain Transactions Involving Stock Compensation" in accounting for its employee stock option plans. According to APB 25, compensation expense is measured under the intrinsic value method, whereby compensation expense is equal to the excess, if any, of the quoted market price of the stock at the grant date of the award or other measurement date over the exercise price.

The following pro forma information presents the effect on the company's and subsidiaries' stock-based employee compensation expense, consolidated net loss and loss per share as if the fair value based method provided under FASB statement No. 123 had been applied to all outstanding awards in each period.

Under SFAS 123 the fair value of each option grant was estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions in all periods presented: (1) expected life of the option of 1-4 years; (2) dividend yield of 0%; (3) expected volatility of 43% (4) risk-free interest rate of 1.5%.

	For the three months ended March 31, 2003 (Unaudited)	For the three months ended March 31, 2002(*) (Unaudited)	For the year ended December 31, 2002 (Audited)
Net loss, as reported	$ (8,611)	$ (8,261)	$ (39,301)
Add: Stock-based employee compensation expense included in reported net loss	227	223	933
Deduct: Total stock-based compensation expense determined under fair value based method for all awards	(353)	(533)	(2,876)
Pro forma net loss	$ (8,737)	$ (8,571)	$ (41,244)
Loss per share:			
Basic and diluted – as reported	$ (0.30)	$ (0.39)	$ (1.50)
Basic and diluted – pro forma	$ (0.30)	$ (0.40)	$ (1.57)

(*) Restated - See Note 3(D).

Note 6 - CONTINGENT LIABILITIES

There were no material changes in the status of the Company's contingent liabilities as described in the annual report for 2002, 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 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 8, 1999, the Company received a copy of a claim and 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 Elron and its officers, among others, relate to the period prior to the sale of Elron's holding in Elbit Medical Imaging ("EMI"). 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 17, 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 new claim similar to the previous one but not as a class action.

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.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

In thousands of U.S. Dollars
(Unaudited)

Note 7 - BUSINESS SEGMENTS

The Company is operating through its subsidiaries, Elron Software Inc. and Elron Telesoft Inc., in two business segments: the internet product segment and the system and projects segment. A third business segment is the Corporate Operation and Other Holdings in affiliated and other companies engaged in various fields of advanced technology and the corporate operation.

The operations of the internet product segment include development and marketing of network management software products, which enable organizations to manage the access to the internet network and to control the incoming and outgoing internet content.

The operation of the system and projects segment includes development and supply of software solutions for the management of large and complex communication and internet networks.

The third segment includes holdings in various companies that operate in the communications, software, defense industry, medical devices, semiconductors, amorphous metals and other fields and the corporate operations.

Segment information is as follows**:**

	Internet Products	Systems and Projects	Holdings (including corporate headquarters)	Adjustments	Total
For the three months ended March 31, 2003:					
Net revenues	$ 1,804	$ 2,074	$ 1,713	$ -	$ 5,591
Net loss	(1,808)	(562)	(6,241)	-	(8,611)
As of March 31, 2003:					
Total assets	5,940	16,287	376,441	(12,837)(**)	385,831
For the three months ended March 31, 2002(*):					
Net revenues	$ 1,871	$ 4,035	$ -	$ -	$ 5,906
Net loss	(2,686)	(642)	(4,933)	-	(8,261)
For the year ended December 31, 2002					
Net revenues	$ 8,290	$ 10,069	$ 5,109	$ -	$ 23,468
Net loss	(8,567)	(5,912)	(24,822)	-	(39,301)
As of December 31, 2002:					
Total assets	6,057	17,601	390,344	(12,673)(**)	401,329

(*) Restated - See Note 3(D).
(**) Inter-company balances.

In thousands of U.S. Dollars

Note 8 - 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:

For the three months ended March 31, 2003 (unaudited):

	As reported	Adjustments	As per Israeli GAAP
Net loss	$ (8,611)	$ 521	$ (8,090)
Basic and diluted net loss per share	(0.30)	0.02	(0.28)

For the three months ended March 31, 2002 (unaudited):

	As Reported (*)	Adjustments	As per Israeli GAAP
Net loss	$ (8,261)	$ 191	$ (8,070)
Basic and diluted net loss per share	(0.39)	-	(0.39)

(*) Restated - See Note 3(D).

For the year ended December 31, 2002 (audited):

	As reported	Adjustments	As per Israeli GAAP
Net loss	$ (39,301)	$ 933	$ (38,368)
Basic and diluted net loss per share	(1.50)	0.04	(1.46)

B. Effect on the balance sheet:

As of March 31, 2003 (unaudited):

	As reported	Adjustments	As per Israeli GAAP
Total assets	$ 385,831	$ (124,686)	$ 261,145
Total liabilities including minority interest	130,466	(26,434)	104,032
Total equity	255,365	(98,252)	157,113

As of December 31, 2002 (audited):

	As reported	Adjustments	As per Israeli GAAP
Total assets	$ 401,329	$ (129,064)	$ 272,265
Total liabilities including minority interest	134,812	(27,462)	107,350
Total equity	266,517	(101,602)	164,915

Note 8 - RECONCILIATION TO ISRAELI GAAP (Cont.)

C. MATERIAL ADJUSTMENTS:

The abovementioned adjustments result primarily from the differences between U.S. GAAP and Israeli GAAP as detailed in Note 26 to the Company's annual financial statements for the year ended 2002.

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ELRON ELECTRONIC INDUSTRIES LTD.

AND ITS SUBSIDIARIES

ANNEX TO THE CONSOLIDATED FINANCIAL STATEMENTS

In thousands of U.S. Dollars

Details relating to major investments as of March 31, 2003:

	% Outstanding shares	Carrying value of the investment March 31, 2003 [1]	Market value of the publicly traded investments as of: March 31, 2003	May 19, 2003
Consolidated Companies:				
Elron Software Inc.	96%	$ (1,052)	$ -	$ -
Elron Telesoft Inc.	99%	9,863	-	-
Galil Medical Ltd. [2]	33%	4,588	-	-
MediaGate N.V.	68%	(448)	-	-
Affiliated Companies (equity):				
Elbit Systems Ltd. (Nasdaq: ESLT)	20%	85,429	129,971	138,177
Given Imaging Ltd. (Nasdaq: GIVN) [2]	18%	25,324	39,673	36,480
NetVision Ltd.	46%	854	-	-
Wavion Inc.	45%	701	-	-
Kidum Elron IT (KIT) Ltd.	29%	573	-	-
Chip Express Corporation	33%	4,389	-	-
Pulsicom Israel Technologies Ltd.	17%	709	-	-
3DV Systems Ltd. [2]	25%	679	-	-
Advanced Metal Technologies Ltd. (AMT)	28%	4,078	-	-
Witcom Ltd. [2]	20%	472	-	-
CellAct Ltd.	45%	299	-	-
Semiconductors Engineering Laboratories Ltd. (SELA) [2]	25%	610	-	-
Ingeneo Ltd. [2]	21%	368	-	-
Notal Vision Ltd.	25%	1,659	-	-
Available for sale:				
Partner Communications Company Ltd. (Nasdaq: PTNR)	12%	74,594	74,594	92,745
24/7 Real Media (Nasdaq: TFSM)	11%	2,380	2,380	3,224
Partnership:				
Gemini Israel Fund	5%	263	-	-
InnoMed	14%	2,003	-	-
Cost:				
Oren Semiconductor Inc.	17%	8,624	-	-

(1) Includes loans and convertible notes.

(2) Represents the carrying value and the percentage holding of the investment in Elron's books and Elron's share in the carrying value and percentage holding of the investment in RDC's books.