

SCAILEX CORPORATION LTD.

(An Israeli Corporation)

INTERIM REPORT

(UNAUDITED)

AT SEPTEMBER 30, 2006

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The amounts are stated in U.S. dollars (\$) in thousands.

November 20, 2006

The Board of Directors of
Scailex Corporation Ltd.
Tel Aviv.

Dear Sirs,

Re: Review of condensed consolidated unaudited interim financial statements for the nine and three month periods ended September 30, 2006.

At your request, we have reviewed the condensed consolidated interim balance sheet of Scailex Corporation Ltd. (hereafter - the Company) and its subsidiaries as of September 30, 2006, the condensed consolidated statements of operations for the nine and the three month periods ended on that date, and the condensed consolidated statements of changes in shareholders' equity and cash flows for the nine month period ended on that date. Our review was performed in accordance with the procedures prescribed by the Institute of Certified Public Accountants in Israel. Inter-alia, these procedures included: reading the financial statements referred to above, reading the minutes of meetings of shareholders and of the board of directors and its committees and making inquiries of Company 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 condensed consolidated interim financial statements.

In performing our review, nothing came to our attention that indicates that material adjustments need be made to the interim condensed consolidated financial statements referred to above, in order for them to be considered as having been prepared in accordance with accounting principles generally accepted in the United States of America and in accordance with the SEC regulations for interim statements (Regulation S-X: Item 210.10-01).

Sincerely yours,

Kesselman & Kesselman
Certified Public Accountants (Isr.)

SCAILEX CORPORATION LTD.

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CONDENSED CONSOLIDATED BALANCE SHEETS

AT SEPTEMBER 30, 2006

	<u>September 30, 2006</u>	<u>December 31, 2005</u>
	<u>(Unaudited)</u>	<u>(Audited)</u>
	<u>U.S. dollars in thousands</u>	
A s s e t s		
CURRENT ASSETS:		
Cash and cash equivalents	221,467	200,047
Short-term investments	42,385	30,405
Restricted deposit	-	5,165
Other receivables	795	568
Deferred income taxes	-	1,260
Current assets of discontinued operations	<u>27,824</u>	<u>81,072</u>
T o t a l current assets	<u>292,471</u>	<u>318,517</u>
INVESTMENTS AND OTHER NON-CURRENT ASSETS:		
Securities held-to-maturity	23,988	29,707
Other investments and prepaid expenses	1,064	1,529
Funds in respect of employee rights upon retirement	82	61
Non current assets of discontinued operations	<u>-</u>	<u>1,195</u>
	25,134	32,492
PROPERTY AND EQUIPMENT , net of accumulated depreciation and amortization	<u>7</u>	<u>9</u>
	<u>317,612</u>	<u>351,018</u>

_____))
Eran Schwartz) **Chairman of the Board of Directors**

_____))
Yahel Shachar) **Chief Executive Officer**

	September 30, 2006	December 31, 2005
	<u>(Unaudited)</u>	<u>(Audited)</u>
	<u>U.S. dollars in thousands</u>	
Liabilities and shareholders' equity		
CURRENT LIABILITIES:		
Trade payables	47	73
Income taxes payable	13,673	13,660
Accrued and other liabilities	631	1,142
Current liabilities related to discontinued operation	<u>16,300</u>	<u>31,443</u>
T o t a l current liabilities	<u>30,651</u>	<u>46,318</u>
LONG-TERM LIABILITIES:		
Liability for employee rights upon retirement	168	107
Long-term liabilities related to discontinued operations	<u>1,200</u>	<u>1,800</u>
T o t a l long-term liabilities	<u>1,368</u>	<u>1,907</u>
COMMITMENTS AND CONTINGENT LIABILITIES		
T o t a l liabilities	<u>32,019</u>	<u>48,225</u>
MINORITY INTEREST OF DISCONTINUED OPERATION	<u>10,381</u>	<u>41,190</u>
SHAREHOLDERS' EQUITY:		
Share capital - ordinary shares of NIS 0.12 par value (authorized – September 30, 2006 and December 31, 2005 - 48,000,000 shares; issued and outstanding - September 30, 2006 and December 31, 2005 - 43,467,388 shares)	6,205	6,205
Capital surplus	280,340	280,269
Accumulated other comprehensive loss	(736)	(1,110)
Retained earnings	21,703	8,539
Treasury shares, at cost (September 30, 2006 and December 31, 2005 - 5,401,025 shares)	<u>(32,300)</u>	<u>(32,300)</u>
T o t a l shareholders' equity	<u>275,212</u>	<u>261,603</u>
	<u>317,612</u>	<u>351,018</u>

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

SCAILEX CORPORATION LTD.

(An Israeli Corporation)

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	Nine months ended September 30		Three months ended September 30	
	2006	2005	2006	2005
	(Unaudited)		(Unaudited)	
	U.S. dollars in thousands (except per share data)			
GENERAL AND ADMINISTRATIVE EXPENSES	1,810	1,905	571	657
OPERATING LOSS	1,810	1,905	571	657
FINANCIAL INCOME - net	9,395	2,944	3,482	1,056
OTHER INCOME - net	2,466	938		141
INCOME BEFORE TAXES ON INCOME	10,051	1,977	2,911	540
TAXES ON INCOME	(1,580)	(649)	(184)	(233)
GAIN FROM SALE / SHARE IN RESULTS OF ASSOCIATED COMPANY		2,876		2,000
MINORITY INTERESTS IN RESULTS OF A SUBSIDIARY	(387)		(87)	
NET INCOME FROM CONTINUING OPERATIONS	8,084	4,204	2,640	2,307
NET INCOME (LOSS) FROM DISCONTINUED OPERATION	5,080	3,705	(432)	1,069
NET INCOME FOR THE PERIOD	<u>13,164</u>	<u>7,909</u>	<u>2,208</u>	<u>3,376</u>
EARNINGS (LOSS) PER SHARE (“EPS”) - BASIC:				
Continuing operations	\$0.21	\$0.11	\$0.07	\$0.06
Discontinued operation	\$0.13	\$0.10	\$(0.01)	\$0.03
	<u>\$0.34</u>	<u>\$0.21</u>	<u>\$0.06</u>	<u>\$0.09</u>
EARNINGS (LOSS) PER SHARE (“EPS”) - DILUTED:				
Continuing operations	\$0.21	\$0.11	\$0.07	\$0.06
Discontinued operation	\$0.13	\$0.09	\$(0.01)	\$0.03
	<u>\$0.34</u>	<u>\$0.20</u>	<u>\$0.06</u>	<u>\$0.09</u>
WEIGHTED AVERAGE NUMBER OF SHARES USED IN COMPUTATION OF EPS (in thousands) -				
Basic	<u>38,066</u>	<u>38,066</u>	<u>38,066</u>	<u>38,066</u>
Diluted	<u>38,146</u>	<u>38,134</u>	<u>38,146</u>	<u>38,134</u>

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

SCAILEX CORPORATION LTD.

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CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

	<u>Share capital</u>	<u>Capital surplus</u>	<u>Accumulated other comprehensive income (loss)</u>	<u>Retained earning (Accumulate deficit)</u>	<u>Treasury shares</u>	<u>Total</u>
BALANCE AT JANUARY 1, 2006 (audited)	6,205	280,269	(1,110)	8,539	(32,300)	261,603
CHANGES DURING THE NINE MONTHS ENDED SEPTEMBER 30, 2006 (unaudited):						
Income for the period				13,164		13,164
Other comprehensive loss, in respect of available-for-sale securities			121			121
Realized losses and amortization included in net income			253			253
Total comprehensive Income						<u>13,538</u>
Amortization of deferred stock compensation		71				71
BALANCE AT SEPTEMBER 30, 2006 (unaudited)	<u>6,205</u>	<u>280,340</u>	<u>(736)</u>	<u>21,703</u>	<u>(32,300)</u>	<u>275,212</u>
BALANCE AT JANUARY 1, 2005 (audited)	6,205	278,295	(327)	(97,599)	(32,300)	154,274
CHANGES DURING THE NINE MONTHS ENDED SEPTEMBER 30, 2005 (unaudited):						
Income for the period				7,909		7,909
Other comprehensive loss, in respect of available-for-sale securities			(685)			<u>(685)</u>
Total comprehensive Income						7,224
Amortization of deferred stock compensation		137				137
BALANCE AT SEPTEMBER 30, 2005 (unaudited)	<u>6,205</u>	<u>278,432</u>	<u>(1,012)</u>	<u>(89,690)</u>	<u>(32,300)</u>	<u>161,635</u>

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

SCAILEX CORPORATION LTD.

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CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Nine months ended September 30	
	2006	2005
	(Unaudited)	
	U.S. dollars in thousands	
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income for the period	13,164	7,909
Adjustments to reconcile net income from continuing operations to net cash provided by operating activities:		
Income and expenses not involving cash flows:		
Minority interests in a subsidiary	387	
Gain from sale / Share in results of associated company, net		(2,876)
Depreciation and amortization	3	5
Amortization of deferred stock compensation	71	17
Long-term prepaid expenses		222
Loss (gain) from sale of available-for-sale securities and bonds interests	271	(81)
Accrued severance pay, net	40	2
Capital gain from dividend paid by investments at cost	(1,800)	
Deferred income taxes, net	1,260	508
Gain from other investment		(792)
Changes in operating asset and liability items:		
Decrease (increase) in other receivable	(227)	903
Increase (decrease) in accounts payable and accruals	(524)	298
Net cash provided by continuing operations	12,645	6,115
Net cash provided by (used in) discontinued operation	40,211	(3,986)
Net cash provided by operating activities	<u>52,856</u>	<u>2,129</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Acquisition of available-for-sale/held-to-maturity marketable securities	(17,047)	(13,233)
Proceeds from sale of marketable securities	10,889	7,972
Purchase of fixed assets	(1)	(13)
Dividend paid by investment at cost	2,890	1,006
Restricted deposits	5,165	5,002
Investment in other investments	(625)	(668)
Proceeds from disposal of associated company		1,000
Net cash provided by investing activities from continued operations	1,271	1,066
Net cash used in investing activities from discontinued operations	(27)	(5,189)
Net cash provided by (used in) investing activities	<u>1,244</u>	<u>(4,123)</u>
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net cash used in financing activities from discontinued operations	(32,680)	(3,913)
Net cash used in financing activities	<u>(32,680)</u>	<u>(3,913)</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	21,420	(5,907)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	<u>200,047</u>	<u>85,892</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u><u>221,467</u></u>	<u><u>79,985</u></u>

SCAILEX CORPORATION LTD.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

AT SEPTEMBER 30, 2006

(UNAUDITED)

NOTE 1 - GENERAL

- a. The interim statements of Scailex Corporation Ltd. (hereafter - the Company) as of September 30, 2006 and for the nine and three months period then ended (hereafter - the interim statements) were drawn up in condensed form, in accordance with generally accepted accounting principles applicable to interim statements. The accounting principles applied in preparation of the interim statements are consistent with those applied in the annual financial statements. Nevertheless, the interim statements do not include all the information and explanations required for the annual financial statements.

In management's opinion, interim financial statements reflect all adjustments (consisting only of normal recurring accruals) necessary for a fair presentation of the financial information, in accordance with generally accepted accounting principles, for the reported periods. Results for interim periods are not necessarily indicative of the results to be expected for the entire year.

- b. On November 1, 2005, Scailex Vision (Tel-Aviv) Ltd (hereafter – “SV”) completed the sale of its business to Hewlett-Packard Company (“HP”). Under the terms of the agreement, HP paid approximately \$230 million in cash to SV (subject to certain adjustment under the agreement), of which \$23 million will be retained in escrow for 24 months to cover possible indemnification claims, and \$1 million will be retained in escrow for 12 months, to cover tax liabilities of SV's subsidiaries in 2005. The Company received the amount of \$1 million (and accrued interest) on November 10, 2006. In addition, SV agreed, among other things, not to compete with HP in the business sold for a period of 2 years following the closing. As a result of the transaction, SV recorded in 2005 a net gain of approximately \$123 million. This gain is net of retained liabilities to third-parties, estimated payments provisions for taxes, transaction-related expenses and other fees and expenses.

In April 2006, HP paid SV additional consideration of \$6.56 million to account for a purchase price adjustment mechanism pursuant to the sale agreement. As a result of the additional consideration, the Company recognized an additional gain from discontinued operation of approximately \$2.9 million (net of taxes and minority interests).

On October 27, 2006, HP filed a claim with the escrow agent for the release of \$5.26 million out of the \$23 million that was retained in escrow to cover possible indemnification claims under the agreement. In the claim, HP alleged that it is entitled to indemnification because SV breached certain representations and warranties it made in the agreement. SV rejects these claims and filed a notice of dispute with the escrow agent. However, there is no assurance that SV will be successful in defending its position, in which case the escrow agent may be required to release such funds to HP. SV has sufficient provisions in its books for covering the result of this claim if it is realized.

- c. During the first quarter of 2006 the Company recorded a capital gain of \$1.8 million derived from a dividend received from RealTimeImage Ltd. (hereafter - “RTI”) following the sale of the business of RTI in 2005. The gain is presented in other income in the statement of operations for the nine months period ended September 30, 2006.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

AT SEPTEMBER 30, 2006

(UNAUDITED)

NOTE 1 - GENERAL (continued):

- d. On January 22, 2006 SV approved a distribution of a cash dividend equivalent approximately to the amount available for distribution, following the conclusion of the asset sale agreement with HP. The aggregate net dividend distribution amounted to \$135 million (of which \$101 million were received by the Company) and resulted in the payment of approximately \$0.80 per share to each shareholder and approximately \$0.39 per option/warrant to each option and warrant holder (net of exercise price).
- e. As a result of the conclusion of an IRS audit of the company US subsidiaries for the years 1992-1996, the Company filed on December 2004 amended federal tax returns for the years 1994, 1995 and 1997, requesting a refund of US federal taxes. In July 2006, the Company received the requested refund in the amount of \$12.6M. The Company has already recorded a federal income tax receivable of \$7.8M in discontinued operations in its financial results for the year ended December 31, 2005, and recorded an additional federal income tax gain of \$4.8M in discontinued operations for the nine months period ended September 30, 2006.
- f. On July 18, 2006 the principal shareholders of the Company (Clal Industries and Investments Ltd. and Discount Investments Corporation Ltd.) completed the sale of all the Company shares held by them, representing 49.4% of the company's outstanding share capital to a fully owned subsidiary of Israel Petrochemical Enterprises Ltd. (an Israeli holding company whose shares are traded on Tel-Aviv Stock Exchange).
- g. On August 4, 2006 the Company entered into a management buy out agreement with senior management of Jemtex InkJet Printing Ltd. (hereafter - "Jemtex"), under which the Company sold the majority of its holdings in Jemtex to two senior managers. As a result, the Company's interest in Jemtex was reduced from approximately 75% to 15%. Under the management buy out agreement, the Company converted approximately \$6.7 million out of \$9.7 million of outstanding loans provided by the Company to Jemtex into shares of Jemtex. The remaining \$3.0 million loan is payable to the company over a period of five to seven years, except that the loan will be deemed fully satisfied if \$1.0 million is paid to the Company before the end of 2006. In addition, for so long as the \$3.0 million loan remains outstanding, the Company will have an option to invest \$5.0 million in Jemtex's shares at a pre-investment valuation of Jemtex of \$20.0 million. As a result of this agreement the Company classified Jemtex as discontinued operations.
- h. Effective January 1, 2006 the Company adopted SFAS No. 123 (Revised 2004) "Share-Based Payment" ("SFAS No. 123R") using the Modified Prospective Approach. SFAS No. 123R revises SFAS No. 123, "Accounting for Stock-Based Compensation" ("SFAS No. 123") and supersedes Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB No. 25"). SFAS No. 123R requires the cost of all share-based payments to employees, including grants of employee stock options, to be recognized in the financial statements based on their fair values at grant date, or the date of later modification, over the requisite service period. In addition, SFAS No. 123R requires unrecognized cost (based on the amounts previously disclosed in the pro forma footnote disclosure) related to options vesting after the date of initial adoption to be recognized in the financial statements over the remaining requisite service period.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

AT SEPTEMBER 30, 2006

(UNAUDITED)

NOTE 1 - GENERAL (continued):

Under the Modified Prospective Approach, the amount of compensation cost recognized includes: (i) compensation cost for all share-based payments granted prior to, but not yet vested as of January 1, 2006, based on the grant date fair value estimated in accordance with the provisions of SFAS No. 123 and (ii) compensation cost for all share-based payments granted subsequent to January 1, 2006, based on the grant date fair value estimated in accordance with the provisions of SFAS No. 123R (there were no new grants in the first and second quarter of 2006). Prior to the adoption of SFAS No. 123R, the Company recognized its share-based compensation costs using the straight-line recognition method. Upon adoption, the Company will continue to use the straight line basis over the requisite service period for existing and new grants. The incremental pre-tax share-based compensation expense recognized due to the adoption of SFAS No. 123R for the nine months period ended September 30, 2006 was immaterial. Total share-based compensation expense recognized under SFAS No. 123R, including the incremental pre-tax share-based compensation expense, was \$71,000. No share-based compensation was capitalized in the consolidated financial statements for the nine months period ended September 30, 2006.

- i. On June 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109 (FIN 48). FIN 48 prescribes a recognition threshold and measurement attribute for financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return, and also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company is assessing FIN 48 and has not determined the impact that the adoption of FIN 48 will have on its results of operations.
- j. In September 2006, FASB issued SFAS No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans—an amendment of FASB Statements No. 87, 88, 106, and 132(R)" ("SFAS No. 158"). This standard requires employers to recognize the underfunded or overfunded status of a defined benefit postretirement plan as an asset or liability in their statement of financial position and to recognize changes in the funded status in the year in which the changes occur through accumulated other comprehensive income. Additionally, SFAS No. 158 requires employers to measure the funded status of a plan as of the date of its year-end statement of financial position. The new reporting requirements and related new footnote disclosure rules of SFAS No. 158 are effective for fiscal years ending after December 15, 2006. The new measurement date requirement applies for fiscal years ending after December 15, 2008. The Company is currently assessing the impact that adoption of SFAS No. 158 will have on its financial statements.
- k. In September 2006, FASB issued SFAS No. 157, "Fair Value Measurements" ("SFAS No. 157"), which defines fair value, establishes a framework for measuring fair value in accordance with GAAP and expands disclosures about fair value measurements. SFAS No. 157 does not require any new fair value measurements, but provides guidance on how to measure fair value by providing a fair value hierarchy used to classify the source of the information. This statement is effective for the Company beginning July 1, 2008. The Company is currently assessing the impact that adoption of SFAS No. 157 will have on its financial statements.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

AT SEPTEMBER 30, 2006

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NOTE 2 - SUBSEQUENT EVENT

On November 9, XMPie, a minority held company, was sold to Xerox Corporation for approximately \$54 million, of which the Company expects to receive approximately \$1.5 million (including \$0.2 million held in escrow).