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AMERICAN ISRAELI PAPER MILLS LTD

Form 6-K

March 10, 2005

SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

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FORM 6-K  
Report of Foreign Private Issuer  
Pursuant to Rule 13a-16 or 15d-16  
of the Securities Exchange Act of 1934  
For the Month of March 2005

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AMERICAN ISRAELI PAPER MILLS LTD.  
(Translation of Registrant's Name into English)  
P.O. Box 142, Hadera, Israel  
(Address of Principal Corporate Offices)

Indicate by check mark whether the registrant files or will file annual reports under cover of Form 20-F or Form 40-F:

Form 20-F                       Form 40-F

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(1):

Note: Regulation S-T Rule 101(b)(1) only permits the submission in paper of a Form 6-K if submitted solely to provide an attached annual report to security holders.

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(7):

Note: Regulation S-T Rule 101(b)(7) only permits the submission in paper of a Form 6-K submitted to furnish a report or other document that the registrant foreign private issuer must furnish and make public under the laws of the jurisdiction in which the registrant is incorporated, domiciled or legally organized (the registrant's "home country"), or under the rules of the home country exchange on which the registrant's securities are traded, as long as the report or other document is not a press release, is not required to be and has not been distributed to the registrant's security holders, and, if discussing a material event, has already been the subject of a Form 6-K submission or other Commission filing on EDGAR.

Indicate by check mark whether the registrant by furnishing the information contained in this form is also thereby furnishing the information to the Commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934:

Yes                                       No

If "Yes" is marked, indicate below the file number assigned to the registrant in connection with Rule 12g3-2(b): 82-\_\_\_\_\_

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Attached hereto as Exhibit 1 and incorporated herein by reference is the Registrant's press release dated March 10, 2005 with respect to the Registrant's results of operations for the year ended December 31, 2004.

Attached hereto as Exhibit 2 and incorporated herein by reference is the Registrant's Management Discussion with respect to the Registrant's results of operations for the year ended December 31, 2004.

Attached hereto as Exhibit 3 and incorporated herein by reference are the Registrant's unaudited condensed consolidated financial statements for the year ended December 31, 2004.

Attached hereto as Exhibit 4 and incorporated herein by reference is the Interim Report of Mondi Business Paper Hadera Ltd. with respect to the year ended December 31, 2004.

Attached hereto as Exhibit 5 and incorporated herein by reference are the unaudited condensed interim consolidated financial statements of Hogla-Kimberly Ltd. and subsidiaries with respect to the year ended December 31, 2004.

### SIGNATURE

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Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

AMERICAN ISRAELI PAPER MILLS LTD.  
(Registrant)

By: /s/ Lea Katz

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Name: Lea Katz

Title: Corporate Secretary

Dated: March 10, 2005.

### EXHIBIT INDEX

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Exhibit No. -----	Description -----
1.	Press release dated March 10, 2005.
2.	Registrant's management discussion.
3.	Registrant's unaudited condensed consolidated financial statements.
4.	Interim report of Mondi Business Paper Hadera Ltd.
5.	Unaudited condensed interim consolidated financial

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statements of Hogla-Kimberly Ltd. and subsidiaries.

EXHIBIT 1

NEWS

Client: AMERICAN ISRAELI  
PAPER MILLS LTD.

Agency Contact: PHILIP Y. SARDOFF

For Release: IMMEDIATE

American Israeli Paper Mills Ltd.  
Reports Financial Results of Fiscal Year Ended December 31, 2004

Hadera, Israel, March 10, 2005 - American Israeli Paper Mills Ltd. (ASE:AIP) (the "Company" or "AIPM") today reported financial results for the year ended December 31, 2004.

Pursuant to the directives of Standard No.12 of the Accounting Israeli Standards Board ("Standard 12"), the Company began to report in nominal New Israeli Shekels (NIS) as of January 1, 2004. In the past, the Company's reports were in NIS, adjusted to changes in the exchange rate of the US dollar against the NIS.

The comparison figures with the corresponding periods of 2002 and 2003 are the dollar figures, as reported in the past, multiplied by the exchange rate of the US dollar as of December 31, 2003, the day of the transition to NIS-based reporting pursuant to Standard 12 (\$1 = NIS 4.379).

Since the Company's share in the earnings of associated companies constitutes a material component in the Company's statement of income (primarily on account of its share in the earnings of Mondi Business Paper Hadera (Mondi Hadera) and Hogla-Kimberly (H-K) that were consolidated in the past, until the transfer of control over these companies to the international strategic partners), the Company also presents the aggregate data which include the results of all the companies in the AIPM Group (including the associated companies whose results appear in the financial statements under "earnings from associated companies"), net of intercompany sales and irrespective of the percentage of holding.

Aggregate group sales in 2004 totaled NIS 2,626.2 million compared with NIS 2,357.1 million in 2003.

Aggregate operating profit in 2004 totaled NIS 143.5 million compared with NIS 162.8 million in 2003.

The consolidated data below does not include the results of operations of Mondi Hadera, H-K, Carmel Container Systems and TMM Integrated Recycling industries, which are included in the Company's share in results of associated companies.

Consolidated sales in 2004 totaled NIS 482.9 million compared with NIS 465.1 in 2003.

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The Gross margin - as a proportion of sales - reached 22.1% during 2004, similar to 2003. The Company managed to maintain the consolidated gross margin, despite the rise in raw material prices (paper waste by 13%), energy prices (4%), and water (5%). This was accomplished through growth in sales, higher sales prices and the continued efficiency process in all sectors of operation.

Operating profit in 2004 totaled NIS 53.9 million compared with NIS 46.6 million in 2003.

Profit after taxes and before the Company's share in the profits of associated companies in the reported period amounted to NIS 37.7 million compared with NIS 24.5 million in 2003.

Net profit in 2004 totaled NIS 62.7 million, as compared with NIS 60.0 million in 2003. Net profit in 2004 includes non recurring profits, which amounted to NIS 14.4 million tax benefit in respect of the effects of the reduction of the corporate tax rate (from 36% to 30% by 2007) on the deferred tax reserve (at the Company, and our share in associated companies) along with a tax benefit on account of the exercise of options by employees. Net profit in 2003 included approximately NIS 2.7 million in net non-recurring capital gains and tax benefit on account of the exercise of options by employees.

Earnings per share (EPS) in 2004 totaled NIS 15.44 compared with NIS 14.94 in 2003.

The inflation rate in 2004 was 1.2% as compared with negative inflation rate of -1.9% last year.

The exchange rate of the NIS was revaluated against the U.S. dollar in 2004 by approximately 1.6% as compared with a revaluation of 7.6% last year.

Mr. Yaacov Yerushalmi, Chairman of the Company's Board of Directors, said that a turnaround took place in the Israeli economy since the beginning of 2004, as growth recovered and the economy rebounded, following a severe recession that lasted several years. The recovery was expressed by positive growth rates (approximately 4% in 2004, up from 1.3% in 2003), higher demand and a more optimistic outlook in the markets. Israel has also experienced a certain calm in the security situation lately, which may positively affect the economy, although this calm is not yet reflected in the financial statements.

The Company is exposed to competition in all its areas of operation, both from locally-produced goods and from imports. The level of competition is constantly escalating. Despite this competition, the Group is successfully preserving the profitability of its Israeli operations, while recording continued growth in the volume of operations.

The Company's share in the earnings of associated companies amounted to NIS 25.1 million in the reported year (including NIS 4.4 million as our share in a non-recurring benefit recorded in respect of the change in the corporate tax rate on the deferred earnings of the companies), as compared with NIS 35.5 million last year.

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The following principal changes were recorded in the Company's share in the earnings of associated companies (this year - not including the aforementioned tax benefit), in relation to last year:

- The Company's share in the net income of Mondi Hadera (49.9%)

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decreased by NIS 3.0 million. Most of the change in the earnings is associated with a decrease in operating profit over the two years, which originated primarily from lower margins in exports to Europe, coupled with elevated financial expenses this year as a result of the repayment of shareholder loans over the past two years, that led to an increase in Mondi Hadera's debt balance.

- The Company's share in the net earnings of H-K Israel (49.9%) increased by approximately NIS 1.2 million, primarily due to the ongoing improvement in operating profit at H-K Israel, as compared with last year. This improvement was achieved primarily as a result of better prices and quantitative growth, coupled with the continuing efficiency measures, both in logistics and in production, and particularly as a result of the expanded production of Huggies diapers in Afula. The said increase was offset by lower financial revenues this year as compared with last year, due to the transition to reporting according to Standard 12 and the effects of revaluation differentials on the NIS in relation to the USD, on H-K's linkage balance sheet.

- The Company's share in the net loss of Ovisan (Turkey) (49.9%) amounted to NIS 15.4 million in the reported year. Ovisan made considerable efforts to increase its volume of operations in the Turkish market during the past year, while tapping into Unilever's nationwide distribution network, which includes a wide logistic network that covers all of Turkey in wide national spread, as a necessary condition for the preparations for the continued development of Ovisan and the creation of a platform for introducing the Kimberly-Clark Group's international brands. In this capacity, a significant quantitative increase was recorded this year in the Ovisan sales - both to the domestic market and to export (up about 40% quantitatively) - accompanied by a significant increase in selling and advertising expenses. The Ovisan loss during the reported year was caused as a result of the said change in the Ovisan distribution and sales network, coupled with escalating competition in the Turkish market due to the arrival of additional competitors into the sector, which resulted in lower prices and a need to adjust the value of inventories to the market prices on the balance sheet date. The difficulties that were created in the assimilation of the new reporting system, which accompanied the change in the distribution system, resulted in delays in receiving the data and in difficulties in providing an immediate response to changing market conditions and in reducing the losses, as mentioned above.

- The Company's share in the net profits of the Carmel Group (26.25%) increased by NIS 3.6 million, due to the continuing improvement in the operating profit. The improvement is attributed to the comprehensive efficiency measures being initiated by the company, coupled with the growth in the volume of operations.

- The Company's share in the TMM earnings (41.6%) increased by NIS 1.3 million. The improvement originates from a significant

decrease in the company's elevated financial expenses during the reported year, in relation to last year. Among other factors, this is attributed to a decrease in the interest rate over the two periods, coupled with financial revenues from local municipalities (with which an agreement was reached) due to considerable arrears in their payments. TMM managed to preserve its operating margin during the reported year, despite the considerable increase in transportation costs, due to the significant increase in diesel prices (up by an average of 40% since last year), which was not compensated by selling prices since most of the company's

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agreements are linked to the consumer price index which rose during 2004 by only 1.2%.

A total of 28,379 shares were issued during the reported year (0.7% dilution), as a result of the exercise of 64,140 option warrants as part of the Company's employee stock option plans.

In August, the Company declared a dividend payment for 2004, in the amount of approximately NIS 100 million (NIS 25.12 per share). The dividend was paid in September 2004.

This report contains various forward-looking statements based upon the Board of Directors' present expectations and estimates regarding the operations of the Group and its business environment. The Company does not guarantee that the future results of operations will coincide with the forward-looking statements and these may in fact differ considerably from the present forecasts as a result of factors that may change in the future, such as changes in costs and market conditions, failure to achieve projected goals, failure to achieve anticipated efficiencies and other factors which lie outside the control of the Company. The Company undertakes no obligation for publicly updating the said forward-looking statements, regardless of whether these updates originate from new information, future events or any other reason.

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AMERICAN ISRAELI PAPER MILLS LTD.  
SUMMARY OF RESULTS  
(AUDITED)  
NIS IN THOUSANDS(1)  
except per share amounts

	2004 =====	2003 =====
Net sales	482,854	465,092
Net earnings	62,732(2)	60,047(2)
Earnings per share	1,544(2)	1,494(2)

- (1) New Israeli Shekel amounts are reported according to Accounting Standard No. 12 of the Israeli Accounting Standard Board (hereafter - Standard No. 12) - "Discontinuance of Adjusting Financial Statements for Inflation". The reported NIS under Standard No. 12 are nominal NIS, for transactions made after January 1, 2004. The amounts of 2003 have been adjusted to reflect changes in the rate of exchange between the U.S. dollar and the New Israeli Shekel until the end of December 2003 (date of transition to Standard No. 12).

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The representative exchange rate at December 31, 2004 was NIS 4.308=\$1.00 and the representative exchange rate at December 31, 2003 was NIS 4.379=\$1.00.

- (2) The net earnings in 2004 include NIS 14.4 million, tax benefit (including the company's share in the tax benefit of the associated companies) - see above.

The net earnings in 2003 include NIS 2.7 million, net capital gain and tax benefit - See above.

(sec-pres-21109)

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EXHIBIT 2

March 10, 2005

### MANAGEMENT DISCUSSION

We are honored to present the consolidated financial statements of the American Israeli Paper Mills Ltd. Group ("AIPM") for the year 2004.

#### A. A SUMMARIZED DESCRIPTION OF THE GROUP AND ITS BUSINESS ENVIRONMENT

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##### 1. GENERAL

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AIPM deals in the manufacture and sale of paper, in the recycling of paper waste and in the marketing of office supplies - through subsidiaries. AIPM also holds interests in associated companies that deal in the manufacture and marketing of printing and writing paper, in the manufacture and marketing of household paper products, hygiene products, disposable diapers and complementary kitchen products, corrugated board containers, packaging for consumer goods and the handling of solid waste.

The company's securities are traded on the Tel Aviv Stock Exchange and on the American Stock Exchange (AMEX).

##### 2. THE BUSINESS ENVIRONMENT

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A turnaround took place in the Israeli economy since the beginning of 2004, as growth recovered and the economy rebounded, following a severe recession that lasted several years. The recovery was expressed by positive growth rates (approx. 4% in 2004, up from 1.3% in 2003), higher demand and a more optimistic outlook in the markets. Israel has also experienced a certain calm in the security situation lately, which may positively affect the economy, although this calm is not yet

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reflected in the financial statements.

AIPM is exposed to competition in all its areas of operation, both from locally-produced goods and from imports. The level of competition is constantly escalating.

Despite this competition, the Group is successfully preserving the profitability of its Israeli operations, while recording continued growth in the volume of operations.

AIPM is preparing for the conversion of its energy-generation system to natural gas, once the transportation infrastructure of natural gas to Hadera is completed. This conversion is expected to enable savings in production costs, while further improving environmental compliance.

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AIPM made the transition to reporting in nominal New Israeli Shekels (NIS) in 2004, pursuant to the directives of Standard 12 of the Financial Accounting Standards Board in Israel. In the past AIPM's reports were in NIS, adjusted to changes in the exchange rate of the US dollar against the NIS. The comparison figures with the years 2003 and 2002 are the dollar figures, as reported in the past, multiplied by the exchange rate of the US dollar as at December 31, 2003, the day of the transition to NIS-based reporting pursuant to Standard 12 (\$1 = NIS 4.379).

The exchange rate of the NIS in relation to the USD was revaluated by 1.6% during the reported year (2004), as compared with a revaluation of 7.6% last year (2003).

The inflation rate during the reported year amounted to 1.2%, as compared with a negative inflation rate of -1.9% last year.

### B. RESULTS OF OPERATIONS

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#### 1. AGGREGATE DATA

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Since AIPM's share in the earnings of associated companies constitutes a material component in the company's statement of income (primarily on account of its share in the earnings of Mondi Business Paper Hadera Ltd. (hereinafter: "Mondi Hadera", formerly - Neusiedler Hadera Paper Ltd. and Hogla-Kimberly Ltd. that were consolidated in the past, until the transfer of control over these companies to the international strategic partners), the aggregate data is being presented and includes the results of all the companies in AIPM (including the associated companies whose results appear in the financial statements under "earnings from associated companies") and net of intercompany sales, without considering the rate of holding therein.

The aggregate sales amounted to NIS 2,626.2 million during the reported year, as compared with NIS 2,357.1 million last year.

The aggregate operating profit totaled NIS 143.5 million during the



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reported year, as compared with NIS 162.8 million last year.

### 2. CONSOLIDATED DATA

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Excluding the results of operation of Mondi Hadera, Hogla-Kimberly, Carmel and TMM - which appear in AIPM's share in the earnings of associated companies.

The sales amounted to NIS 482.9 million during the reported year, as compared with NIS 465.1 million last year.

The operating profit this year amounted to NIS 53.9 million, as compared with NIS 46.6 million last year.

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The profit after taxes and before AIPM's share in the earnings of associated companies for the reported year, amounted to NIS 37.7 million, as compared with NIS 24.5 million last year.

### 3. NET PROFIT AND EARNINGS PER SHARE

-----  
The net profit amounted to NIS 62.7 million during the reported year, as compared with NIS 60.0 million last year. The net profit during the reported year includes extraordinary earnings on account of a NIS 14.4 million tax benefit, originating from the influence of the lowering of the corporate tax rate on the reserve for deferred taxes at AIPM and at its associated companies (from 36% to 30% by 2007), along with a tax benefit on account of the exercise of options by employees. The net profit last year included NIS 2.7 million in non-recurring capital gains and in a tax benefit on account of the exercise of options by employees.

The Earnings Per Share in 2004 amounted to NIS 1,544 per NIS 1 par value (\$3.58 per share), as compared with NIS 1,494 per NIS 1 par value (\$3.41 per share) in 2003.

The return on shareholders' equity amounted to 10.2% in 2004, as compared with 9.2% in 2003.

## C. ANALYSIS OF OPERATIONS AND PROFITABILITY

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The analysis set forth below is based on the consolidated data.

### 1. SALES

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The consolidated sales amounted to NIS 482.9 million during the reported year, as compared with NIS 465.1 million last year.

The growth in sales is attributed to a quantitative increase in packaging paper and in the sale of paper waste to external entities, coupled with an improvement in the prices of fluting and paper waste and a change in the sales mix. On the other hand, the decrease in

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Graffiti sales served to offset part of this growth.

### 2. COST OF SALES

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The cost of sales amounted to NIS 375.9 million during the reported year, as compared with NIS 362.2 million last year.

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The gross margin - as a proportion of sales - reached 22.1% during the reported year and is similar to last year.

AIPM managed to maintain a gross margin similar to last year, despite the rise in raw material prices (paper waste by 13%), energy prices (4%), and water (5%). This was accomplished through growth in sales, higher sales prices and the continued efficiency process in all sectors of operation.

#### LABOR WAGES

Wages as part of the cost of sales and in the selling, general and administrative expenses amounted to NIS 142.4 million in the reported year, as compared with NIS 137.0 million last year.

However, since the figures last year were reported in accordance with the US dollar and due to the influence of changes in the exchange rate of the US dollar on the reporting last year with the transition to reporting according to Standard 12, the adjusted cost of wages last year, as presented above, was NIS 3.7 million lower than the nominal cost at the time that amounted to NIS 140.7 million. Most of the growth in relation to last year originated from an increase in wages by an average of 3%, that was mostly offset by a reduction in personnel and by differences in other payments - primarily bonuses.

### 3. SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

-----  
The selling, general and administrative expenses (including wages) amounted to NIS 53.0 million - or 11.0% of sales - in the reported year, as compared with NIS 56.3 million - or 12.1% of sales - last year.

### 4. OPERATING PROFIT

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The operating profit amounted to NIS 53.9 million - or 11.2% of sales - in the reported year, as compared with NIS 46.6 million - or 10.0% of sales - last year.

### 5. FINANCIAL EXPENSES

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Financial expenses amounted to NIS 13.1 million during the reported year, as compared with NIS 16.0 million last year.

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AIPM's linkage bases includes a surplus of dollar-linked monetary assets on the one hand, and a surplus of NIS-denominated monetary liabilities, on the other hand (see linkage base report, below).

The financial expenses last year were influenced by the sharp revaluation of the shekel against the dollar (7.6%), which caused a significant increase in the financial expenses during the said period, when financial reporting was adjusted to the dollar.

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In the reported year, with the transition to reporting in nominal shekels in accordance with Standard 12, AIPM's financial expenses grew slightly, as a result of the effects of the small revaluation this year (1.6%) on AIPM's surplus dollar assets.

The average increase of NIS 60 million in net financial liabilities - in relation to the preceding year - resulted in an increase in financial expenses during the reported year. This growth was partially offset by the decrease in the average interest rate on short-term credit (5% in the reported year as compared with 7.9% last year).

### 6. TAXES ON INCOME

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Taxes on income from current operations amounted to NIS 13.2 million in the reported period, as compared with NIS 8.8 million last year.

The principal factors behind the growth in tax expenses in the reported year as compared with last year include the growth in earnings before taxes this year, as opposed to the tax benefit that was recorded last year on account of the sharp revaluation (erosion of the reserve), due to reporting adjusted to the changes in the exchange rate of the dollar.

In June 2004 a law was passed in Israel, effective retroactively from January 1, 2004, that serves to lower the corporate tax rate (36% prior to the amendment) to 35% in 2004 and gradually down to 30% by 2007. The effect of this change on AIPM's deferred taxes during the reported year (in the consolidated report) amounted to NIS 5.8 million (primarily due to future tax liabilities which were deferred in respect of timing differences in depreciation, which were calculated at an accelerated pace in the tax reports).

Moreover, a tax benefit of NIS 4.2 million was recorded in the reported year, on account of the exercise of options by employees.

In view of the above, the tax expenses during the reported year, as reported in the financial statements, amounted to NIS 3.2 million.

### 7. PROFIT AFTER TAXES AND PRIOR TO AIPM'S SHARE IN THE EARNINGS OF

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ASSOCIATED COMPANIES

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The profit after taxes and before AIPM's share in the earnings of associated companies for the reported year, amounted to NIS 37.7 million, as compared with NIS 24.5 million last year.

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### 8. AIPM'S SHARE IN EARNINGS OF ASSOCIATED COMPANIES

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The companies whose earnings are reported under this item (according to AIPM's holdings therein), include primarily: Mondri Hadera, Hogla-Kimberly, Carmel and TMM.

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AIPM's share in the earnings of associated companies amounted to NIS 25.1 million in the reported year (including NIS 4.4 million as our share in a non-recurring benefit recorded in respect of the change in the corporate tax rate on the deferred earnings of the companies), as compared with NIS 35.5 million last year.

The following principal changes were recorded in AIPM's share in the earnings of associated companies (this year - not including the aforementioned tax benefit), in relation to last year:

- AIPM's share in the net income of Mondri Hadera (49.9%) decreased by NIS 3.0 million. Most of the change in the earnings is associated with a decrease in operating profit over the years, that originated primarily from lower margins in exports to Europe, coupled with elevated financial expenses this year as a result of the repayment of shareholder loans over the past two years, that led to an increase in Mondri Hadera's debt balance.
- AIPM's share in the net earnings of Hogla-Kimberly Israel (49.9%) increased by approximately NIS 1.2 million, primarily due to the ongoing improvement in operating profit at Hogla-Kimberly Israel, as compared with last year. This improvement was achieved primarily as a result of better prices and quantitative growth, coupled with the continuing efficiency measures, both in logistics and in production, and particularly as a result of the expanded production of Huggies diapers in Afula. The said increase was offset by lower financial revenues this year as compared with last year, due to the transition to reporting according to Standard 12 and the effects of revaluation differentials on the NIS in relation to the USD, on Hogla's linkage balance sheet.
- AIPM's share in the net loss of Ovisan (Turkey) (49.9%) amounted to NIS 15.4 million in the reported year. Ovisan made considerable efforts to increase its volume of operations in the Turkish market during the past year, while tapping into Unilever's nationwide distribution network, which includes a wide logistic network that covers all of Turkey in a wide national spread, as a necessary condition for the preparations for the continued development of Ovisan and the creation of a platform for introducing the Kimberly-Clark Group's international brands. In this capacity, a significant quantitative increase was recorded this year in the Ovisan sales - both to the domestic market and to exports (up about 40% quantitatively) - accompanied by a significant increase in selling and advertising expenses. The Ovisan loss during the reported year was caused as a result of the said change in the Ovisan distribution and sales network, coupled with escalating competition in the Turkish market due to the arrival of additional competitors into the sector, which

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resulted in lower prices and a need to adjust the value of inventories to the market prices on the balance sheet date. The difficulties that were created in the assimilation of the new reporting

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system, which accompanied the change in the distribution system, resulted in delays in receiving the data and in difficulties in providing an immediate response to changing market conditions in reducing the losses, as mentioned above.

- AIPM's share in the net profits of the Carmel Group (26.25%) increased by NIS 3.6 million, due to the continuing improvement in the operating profit. The improvement is attributed to the comprehensive efficiency measures being initiated by the company, coupled with the growth in the volume of operations.
- AIPM's share in the TMM earnings (41.6%) increased by NIS 1.3 million. The improvement originates from a significant decrease in the company's elevated financial expenses during the reported year, in relation to last year. Among other factors, this is attributed to a decrease in the interest rate over the two periods, coupled with financial revenues from local municipalities (with which an agreement was reached) due to considerable arrears in their payments. TMM managed to preserve its operating margin during the reported year, despite the considerable increase in transportation costs, due to the significant increase in diesel prices (up by an average of 40% since last year) which was not compensated by selling prices since most of the company's agreements are linked to the consumer price index which rose during 2004 by only 1.2% .

### D. LIQUIDITY AND INVESTMENTS

#### 1. ACCOUNTS RECEIVABLE - TRADE

Accounts Receivable, as at December 31, 2004, amounted to NIS 143.3 million, as compared with NIS 141.0 million at December 31, 2003. The increase in receivables originated primarily from the growth in the volume of operations. A certain decrease was recorded in the customer credit days.

#### 2. CASH FLOWS

The cash flows from operating activities amounted to NIS 47.1 million this year, as compared with NIS 36.3 million last year. (The NIS 36.3 million in cash flows last year is prior to a NIS 16.4 million dividend received from an associated company. Together with the said dividend, the cash flows from operating activities amounted to NIS 52.7 million last year). The improvement in the cash flows from operating activities during the reported year originated primarily from a smaller increase in the operating working capital during the reported year in relation to last year, despite the growth in operating volumes this year.

3. INVESTMENTS IN FIXED ASSETS  
-----

Investments in fixed assets totaled NIS 31.0 million in the reported year, as compared with NIS 29.2 million last year and included current investments in production, marketing and transport processes as well as in the expansion of information security operations in Israel.

4. FINANCIAL LIABILITIES  
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The long-term liabilities (including current maturities) amounted to NIS 267.9 million as at December 31, 2004 as compared with NIS 275.0 million as at December 31, 2003. The long-term liabilities include primarily two series of debentures: Series 1 - NIS 33.3 million, for repayment until 2009. Series 2 - NIS 201.8 million, for repayment between 2007 and 2013.

The balance of short-term credit, as at December 31, 2004, amounted to NIS 112.7 million, as compared with NIS 144.6 million December 31, 2003. The short-term credit balances decreased in relation to last year, primarily due to the positive cash flows from operating activities. Dividends of NIS 100 million were paid in September 2004. The dividend payment was financed by AIPM's deposits and assets.

E. EXPOSURE AND MANAGEMENT OF MARKET RISKS  
-----

Due to its operations, the company is exposed to market risks, consisting primarily of changes in interest rates - on both short and long-term loans, changes in exchange rates and changes in raw material and energy prices. These changes possess an influence on the company's results. AIPM's Board of Directors determines the policy according to which financial instruments are employed and defines the objectives to be attained, taking into account the AIPM's linkage balance sheet and the impact of changes in various currencies and in the Consumer Price Index on AIPM's balance sheets and on its financial statements.

Mr. Israel Eldar, AIPM's Controller, is in charge of the management of market risks. He conducts calculations of AIPM's exposure every month and examines the compliance with the policy determined by the Board of Directors.

Furthermore, limited use is made of derivative financial instruments, which AIPM's employs for hedging the cash flows, originating from the existing assets and liabilities. Such transactions are conducted primarily through currency options and forward transactions opposite Israeli banking institutions. AIPM therefore believes that the inherent credit risk of these transactions is slight.

AIPM possesses CPI-linked long-term loans (notes) in the total sum of about NIS 235 million, which the interest thereupon being no higher than the market interest rate. In the event that the inflation rate shall rise significantly, a loss may be recorded in AIPM's financial statements, due to the surplus of CPI-linked liabilities. In order to hedge this exposure, AIPM has entered into forward transactions, as at December 31, 2004 for

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hedging NIS 200 million against a rise in the CPI until December 2005.

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These transactions serve to replace hedging transactions in the same amount, that terminated in January 2005.

### CREDIT RISKS

Most of AIPM's sales are made in Israel to a large number of customers and the exposure to customer-related credit risks is consequently generally limited. AIPM regularly analyzes - through credit committees that operate within its various companies - the quality of the customers, their credit limits and the relevant collateral required, as the case may be. The financial statements include provisions for doubtful debts, based on the existing risks on the date of the statements.

The cash, cash equivalents and fixed-term deposits are by and large deposited with large Israeli banking institutions.

The following are the balance sheet items, according to linkage bases, as at December 31, 2004 (including comparison numbers for December 31, 2003):

### REPORT OF LINKAGE BASES

IN NIS MILLIONS	UNLINKED	CPI-LINKED	IN FOREIGN CURRENCY, OR LINKED THERETO (PRIMARYLY US\$)	NON-MO ITEMS
<b>ASSETS</b>				
CASH AND CASH EQUIVALENTS	3.3		4.5	
SHORT-TERM INVESTMENTS	16.9	45.6		
OTHER ACCOUNTS RECEIVABLE	192.0	1.8	43.6	
INVENTORIES				
INVESTMENTS IN ASSOCIATED COMPANIES	49.3	11.2	8.6	3
DEFERRED TAXES ON INCOME				
FIXED ASSETS, NET				3
DEFERRED EXPENSES, NET OF ACCRUED AMORTIZATION				
<b>TOTAL ASSETS</b>	<b>261.5</b>	<b>58.6</b>	<b>56.7</b>	<b>7</b>
<b>LIABILITIES</b>				
CREDIT FROM BANKS	110.5		2.2	
ACCOUNTS PAYABLE	142.8	1.0	10.1	
DEFERRED TAXES ON INCOME				
NOTES		235.1		
OTHER LIABILITIES	32.8			
SHAREHOLDERS' EQUITY				5
<b>TOTAL LIABILITIES AND EQUITY</b>	<b>286.1</b>	<b>236.1</b>	<b>12.3</b>	<b>6</b>

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SURPLUS FINANCIAL ASSETS (LIABILITIES) AS AT DECEMBER 31, 2004	(24.6)	(177.5)	44.4	(15
---	--------	---------	------	-----

SURPLUS FINANCIAL ASSETS (LIABILITIES) AS AT DECEMBER 31, 2003	(69.4)	(229.2)	65.2
---	--------	---------	------

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### ASSOCIATED COMPANIES

AIPM is exposed to various risks associated with operations in Turkey, where Hogla-Kimberly is active through its subsidiary, Ovisan. These risks originate from concerns regarding economic instability and elevated interest rates, that characterized the Turkish economy in the past and that may recur and harm the Ovisan operations.

### F. FORWARD-LOOKING STATEMENTS

This report contains various forward-looking statements, based upon the Board of Directors' present expectations and estimates regarding the operations of AIPM and its business environment. AIPM does not guarantee that the future results of operations will coincide with the forward-looking statements and these may in fact considerably differ from the present forecasts as a result of factors that may change in the future, such as changes in costs and market conditions, failure to achieve projected goals, failure to achieve anticipated efficiencies and other factors which lie outside the control of the company. AIPM undertakes no obligation to publicly update such forward-looking statements, regardless of whether these updates originate from new information, future events or any other reason.

### G. DONATIONS AND CONTRIBUTIONS

AIPM, within the framework of its business and social commitment, invests efforts and resources in community assistance and support, while focusing on providing help to the weaker echelons of Israeli society - and primarily teenagers - as part of a desire to build and contribute to shaping the human fabric of Israeli society. As part of this policy, AIPM makes contributions to various institutions, primarily those that are active in the said areas. These contributions amounted to an adjusted sum of NIS 150 thousand in 2004, in the consolidated financial statements. Through its employees, AIPM also participates in volunteer activity in the community, for promoting these same objectives.

In addition, a sum totaling NIS 90 thousand was granted for student scholarships and social projects this year through the Schenker Foundation, that was established by the company together with its Austrian strategic partner in Mondri Hadera.



H. MEMBERS OF THE BOARD OF DIRECTORS POSSESSING FINANCIAL SKILLS AND  
 -----  
 QUALIFICATIONS  
 -----

The minimum appropriate number of company directors possessing accounting and financial and skills was determined to be two for AIPM, in consideration of the nature of the accounting and financial issues that are raised in the preparation of AIPM's financial statements, in view of AIPM's areas of operation and in consideration of the composition of the board of directors as a whole, that includes individuals possessing business, management and professional experience that enables them to deal effectively with the tasks of managing the company, including reporting duties. The minimum number was also set while taking into account the close accounting counseling that is provided by the company's CPAs, including their participation in board meetings discussing accounting issues and their availability to answer any question put forth by the board of directors.

The members of AIPM's board of directors who possess accounting and financial qualifications and skills are:

- Nochi Dankner - Chairman of the Board of Directors and CEO of IDB Holding Corporation Ltd. Chairman of the Board of Directors of IDB Development Company Ltd., Discount Investments Ltd. and Clal Industries and Investments Ltd. Serves or has served in the past as Chairman of the Board of Directors and Director in publicly-traded and privately-held companies in the Ganden Group, IDB Group, and Bank Hapoalim, where he served as Chairman of the Credit Committee of the Board. Holds L.L.B in Law.
  
- Avi Yehezkel - Holds a degree in economics. External director at Bank Yahav. Served as a Knesset member between 1992-2003, during these years alternately, served as Chairman of the Economics Committee, Chairman of the Defense Budget Committee, Chairman of the Capital Market Sub-Committee, Chairman of the Banking Sub-Committee and member of the Finance Committee.
  
- Oren Lieder - Holds B.A in economics and statistics. Serves as Senior VP and CFO of Discount Investments Ltd. Serves as director at various companies, including publicly-traded companies. Formerly served as CFO of Bezeq, the Israeli Telecom Company Ltd.
  
- Isaac Manor - Holds an MBA. Serves as director at various publicly-traded and privately-held companies within the IDB Group; Chairman of companies in the David Lubinsky Group Ltd.; member of the Accounts Committee at Israel Union Bank Ltd.
  
- Amos Mar-Haim - Holds a first degree in economics and an MBA. Formerly served and currently serves as Chairman or Deputy Chairman at publicly-traded or privately-held

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companies. Member of the Israeli Accounting Standards Board.

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### I. AIPM'S INTERNAL AUDITOR

- 
1. Auditor's Name: Lenny Siegel  
In the position since: 1996  
Credentials: CPA, CA Canadian
  2. The Auditor is employed by AIPM.
  3. Scope of employment: Full-time job as Auditor, plus an assistant.
  4. The auditing program is based on a five-year program that covers numerous topics, in addition to current auditing requirements of the management and directives of the Audit Committee.
  5. The Internal Auditing program includes auditing topics in corporations that constitute significant holdings by AIPM.
  6. The Internal Auditor conducts the audit according to generally-accepted professional standards in Israel and worldwide.
  7. The Internal Auditor is supervised by the Audit Committee and by the General Manager.
  8. Audit reports were submitted and discussed at the following dates:

	SUBMITTED	DISCUSSED
	-----	-----
Report I	March 4, 2004	March 10, 2004
Report II	May 5, 2004	May 10, 2004
Report III	August 8, 2004	August 11, 2004
Report IV	November 7, 2004	November 10, 2004

9. The scope of employment of the Internal Auditor is determined according to a cycle that renders it possible to audit all the significant topics at AIPM, once every few years. This scope of activity, the nature, the continuity of operation and the work plan of the Internal Auditor - are reasonable - according to the estimation of AIPM's Audit Committee, while rendering it possible to realize the Internal Audit objectives of the organization. AIPM declares that it has granted the Internal Auditor free, constant and direct access to all the information that it possesses.

### J. GENERAL

- 
- o In August 2004, AIPM announced the distribution of dividends for 2004, in the amount of NIS 100 million (NIS 25.12 per share). The dividend was paid in September 2004.

- o 28,379 shares were issued during the reported year (0.7% dilution), on account of the exercise of 64,140 option warrants as part of AIPM's employee option plans.
- o Avi Brenner was appointed General Manager of AIPM on January 1, 2005.

-----  
Yaki. Yerushalmi  
Chairman of the Board of Directors

-----  
Avi Brenner  
General Manager

EXHIBIT 3

AMERICAN ISRAELI PAPER MILLS LIMITED  
2004 CONSOLIDATED FINANCIAL STATEMENTS

AMERICAN ISRAELI PAPER MILLS LIMITED  
2004 CONSOLIDATED FINANCIAL STATEMENTS

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AUDITORS' REPORT

To the shareholders of  
AMERICAN ISRAELI PAPER MILLS LIMITED

We have audited the consolidated balance sheets of American Israeli Paper Mills Limited (hereafter - the Company) and its subsidiaries as of December 31, 2004 and 2003 and the related consolidated statements of income, changes in shareholders' equity and cash flows for each of the three years in the period ended December 31, 2004. These financial statements are the responsibility of the Company's board of directors and management. Our responsibility is to express an opinion on these financial statements based on our audits.

We did not audit the financial statements of certain associated companies, the Company's interest in which as reflected in the balance sheets as of December 31, 2004 and 2003 is NIS 353.1 million and NIS 299.3 million, respectively, and the Company's share in excess of profits over losses of which is a net amount of NIS 25.0 million, NIS 28.2 million and NIS 10.2 million for the years ended December 31, 2004, 2003 and 2002, respectively. The financial statements of those companies were audited by other auditors whose reports have been furnished to us, and our opinion, insofar as it relates to amounts included for those companies, is based solely on the reports of the other auditors.

We conducted our audits in accordance with auditing standards generally accepted in Israel and in the standards of the Public Company Accounting Oversight Board (United States), including those prescribed by the Israeli Auditors (Mode of Performance) Regulations, 1973. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the Company's board of directors and management, as well as evaluating the overall financial statement presentation. We believe that our audits and the reports of the other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits and the reports of the other auditors, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company and its subsidiaries as of December 31, 2004 and 2003 and the consolidated results of operations, changes in shareholders' equity and cash flows for each of the three years in the period ended December 31, 2004, in conformity with accounting principles generally accepted ("GAAP") in Israel. Furthermore, in our opinion, the financial statements referred to above have been prepared in accordance with the Israeli Securities (Preparation of Annual Financial Statements) Regulations, 1993.

As explained in note 1b the financial statements, as of dates and for reporting periods subsequent to December 31, 2003, are presented in New Israeli Shekels, in conformity with accounting standards issued by the Israel Accounting Standards Board. The financial statements as of dates and for reporting periods ended prior to, or on the above date, are presented in values that have been adjusted for the changes in the exchange rate of the U.S. dollar, through that date, in accordance with pronouncements of the Institute of Certified Public Accountants in Israel.

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Tel-Aviv, Israel  
March 10 , 2005

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AMERICAN ISRAELI PAPER MILLS LIMITED  
CONSOLIDATED BALANCE SHEETS

	Note	D ----- 2004 ----- NIS in thousa -----
	----	
A s s e t s		
CURRENT ASSETS:	8	
Cash and cash equivalents	1o	7,813
Short-term investments	10a;1f	62,464
Accounts receivable:	10b	
Trade		143,275
Other		101,840
Inventories	10c	83,220
		-----
T o t a l current assets		398,612
		-----
INVESTMENT AND LONG TERM		
RECEIVABLES:		
Investments in associated companies	2;8	431,752
Deferred income taxes	7f	6,511
		-----
		438,263
		-----
FIXED ASSETS:	3	
Cost		974,462
L e s s - accumulated depreciation		650,056
		-----
		324,406
		-----
DEFERRED CHARGES,		
net of accumulated amortization	1i	1,106
		-----
T o t a l assets		1,162,387
		=====

----- ) Chairman of the  
Yaki Yerushalmi ) Board of Directors  
  
----- )  
----- ) Chief Executive Officer  
Avi brener

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----- )  
 Israel Eldar ) Controller

Date of approval of the financial statements: March 10, 2005.

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

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	Note	De ----- 2004 ----- NIS in thous -----
Liabilities and shareholders' equity		
CURRENT LIABILITIES:	8	
Credit from banks	10d	112,
Current maturities of long-term notes	4a	6,
Accounts payable and accruals:		
Trade		87,
Other	10e	66,
T o t a l current liabilities		----- 273,
LONG-TERM LIABILITIES:		
Deferred income taxes	7f	52,
Loans and other liabilities (net of current maturities):	4;8	
Notes		228,
Other liabilities		32,
T o t a l long-term liabilities		----- 313,
COMMITMENTS AND CONTINGENT LIABILITIES	9	
T o t a l liabilities		----- 587,
SHAREHOLDERS' EQUITY:	6	
Share capital (ordinary shares of NIS 0.01 par value: authorized - 20,000,000 shares; issued and paid: December 31, 2004 and 2005 - 3,996,674 and 3,968,295 shares, respectively)		125,
Capital surplus		90,
Currency adjustments in respect of financial statements of associated companies		(2,
Retained earnings		362, 575,
T o t a l liabilities and shareholders' equity		----- 1,162, =====

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

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AMERICAN ISRAELI PAPER MILLS LIMITED  
CONSOLIDATED STATEMENTS OF INCOME

	Note	2004
	-----	-----
		NIS in
SALES - net	10f;14	482,854
COST OF SALES	10g	375,904
		-----
GROSS PROFIT		106,950
		-----
SELLING, MARKETING, ADMINISTRATIVE AND GENERAL EXPENSES:	10h	
Selling and marketing		30,595
Administrative and general		22,425
		-----
		53,020
		-----
INCOME FROM ORDINARY OPERATIONS		53,930
FINANCIAL EXPENSES - net	10i	13,118
OTHER INCOME (EXPENSES)	10j	
		-----
INCOME BEFORE TAXES ON INCOME		40,812
TAXES ON INCOME	7	3,152
		-----
INCOME FROM OPERATIONS OF THE COMPANY AND ITS SUBSIDIARIES		37,660
SHARE IN PROFITS OF ASSOCIATED COMPANIES - net	2	25,072
		-----
NET INCOME FOR THE YEAR		62,732
		=====
		-----
NET INCOME PER NIS 1 OF PAR VALUE OF SHARES	1p;11	1,544
		=====

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

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AMERICAN ISRAELI PAPER MILLS LIMITED  
STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

	Share Capital -----	Capital surplus -----	Curren adjustm in res of fina stateme associ compa -----
	NIS in thousands		
BALANCE AT JANUARY 1, 2002	125,256	90,060	(3,17
CHANGES IN 2002:			
Net income			
Dividend paid			
Currency adjustments in respect of financial statements of associated companies			(30
BALANCE AT DECEMBER 31, 2002	125,256	90,060	(3,48
CHANGES IN 2003:			
Net income			
Dividend paid			
Exercise of employee options into shares	1		
Currency adjustments in respect of financial statements of associated companies			2,36
BALANCE AT DECEMBER 31, 2003	125,257	90,060	(1,12
CHANGES IN 2004:			
Net income			
Dividend paid			
Exercise of employee options into shares	*		
Currency adjustments in respect of financial statements of associated companies			(1,68
BALANCE AT DECEMBER 31, 2004	125,257	90,060	(2,80

\*Represents an amount less than NIS 1,000.

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



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	-----	-----
	NIS in thousands (s)	
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income for the year	62,732	60,047
Adjustments to reconcile net income to net cash provided by operating activities (*)	(15,637)	(7,396)
	-----	-----
Net cash provided by operating activities	47,095	52,651
	-----	-----
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of fixed assets	(30,952)	(29,247)
Short-term investments	(42,000)	(20,000)
Associated companies:		
Granting of loans	(779)	(8,241)
Collection of loans	13,688	21,895
Proceeds from sale of fixed assets	1,001	3,332
	-----	-----
Net cash used in investing activities	(59,042)	(32,261)
	-----	-----
CASH FLOWS FROM FINANCING ACTIVITIES:		
Notes issuance, net of issuance expenses of NIS 800,000		198,909
Consideration in respect of the exercise of options by employees		1
Repayment of long-term loans from banks and others	(383)	(762)
Redemption of notes	(6,666)	(6,770)
Dividend paid	(99,964)	(99,128)
Short-term credit from banks - net	(31,933)	40,606
	-----	-----
Net cash provided by (used in) financing activities	(138,946)	132,856
	-----	-----
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(150,893)	153,246
BALANCE OF CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	158,706	5,460
	-----	-----
BALANCE OF CASH AND CASH EQUIVALENTS AT END OF YEAR	7,813	158,706
	=====	=====

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

(*)	Adjustments to reconcile net income to net cash provided by operating activities: Income and expenses not involving cash flows:	
	Share in profits of associated companies - net	(25,072)
	Dividend received from associated company	

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Depreciation and amortization	28,633
Deferred income taxes - net	(10,096)
Capital losses (gains) on:	
Sale of fixed assets	508
Termination of activities and disposal of assets - net	
Gains on short-term deposits and investments not yet realized	(464)
Linkage and exchange differences on principal of	
long-term loans from banks - net	(26)
Linkage differences on (erosion of) principal of Notes	2,184
Erosion of (linkage differences on) principal of	
long-term loans to associated companies	(721)
Appreciation (erosion) of a long-term capital note granted to	
an associated company	
	-----
	5,054
	-----
Changes in operating asset and liability items:	
Increase in trade receivables	(2,279)
Decrease (increase) in other receivables	
(not include deferred income taxes)	(12,037)
Decrease (increase) in inventories	7,434
Increase (decrease) in trade payables	2,954
Increase (decrease) in other payables and accruals	(6,655)
	-----
	(10,583)
	-----
	(15,637)
	=====
Supplementary cash flow information - cash paid during the year for:	
Taxes on income	3,242
	=====
Interest	20,697
	=====

### Information on activities not involving cash flows:

In 2004, equipment, which the company did not find suitable for its use, was retired. The retirement was made against the cancellation of the loan made available to the supplier in respect of said equipment. The retirement amounted to NIS 1,079,000.

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

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### AMERICAN ISRAELI PAPER MILLS LIMITED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

#### NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies, which, except for the changes required by the transition to nominal financial reporting in 2004 - see b(1) and b(4) below, were applied on a consistent basis, are as follows:

a. General:

- 1) Activities of the Group

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American Israeli Paper Mills Limited (hereafter - the Company) and its subsidiaries and associated companies (hereafter - the Group) are engaged in the production and sale of paper and paper products, including paper recycling activities and handling solid waste. Certain companies are engaged in the marketing of office supplies and in the sale of products produced by others (some of which are not paper or paper products). Most of the Group's sales are made to the local market (Israel). As to information by operating segments, see note 14.

### 2) Use of estimates in the preparation of financial statements

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reporting years. Actual results could differ from those estimates.

### 3) Definitions:

Subsidiaries - companies over which the Company has control and over 50% of the ownership, the financial statements of which have been consolidated with the financial statements of the Company.

Associated companies - investee companies, which are not subsidiaries, over whose financial and operational policy the Company exerts material influence, the investment in which is presented by the equity method. Material influence is deemed to exist when the percentage of holding in said company is 20% or more, unless there are circumstances that contradict this assumption.

Interested parties - as defined in the Israeli Securities (Preparation of Annual Financial Statements) Regulations, 1993.

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## AMERICAN ISRAELI PAPER MILLS LIMITED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (continued):

#### b. Basis of presentation of the financial statements

The Company draws up and presents its financial statements in Israeli currency (hereafter - shekels or NIS).

Commencing in 2004, the adjustment of financial statements in Israel for the changes in the exchange rate of the US dollar was discontinued, and transitory provisions for financial reporting on a nominal basis began being applied, as explained below; notwithstanding the above, the comparative figures included in these financial statements are based on the amounts adjusted for the changes in the exchange rate of the US dollar, as previously reported; in the case of the Company, these figures represented adjustment to inflation by way

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of adjustment of the amounts for the changes in the exchange rate of the US dollar (hereafter - the dollar), see (2) below.

### 1) Transition to nominal financial reporting in 2004

With effect from January 1, 2004, the company has adopted the provisions of Israel Accounting Standard No. 12 - "Discontinuance of Adjusting Financial Statements for Inflation" - of the Israel Accounting Standards Board (hereafter -the IASB) and, pursuant thereto, the company has discontinued, from the aforesaid date, the adjustment of its financial statements for the changes in the exchange rate of the dollar against the shekel.

The amounts adjusted for the changes in the exchange rate of the dollar against the shekel (see (2) below), presented in the financial statements as of December 31, 2003 (hereafter - "the transition date"), were used as the opening balances for the nominal financial reporting in the following periods. Additions made after the transition date have been included in the financial statements at their nominal values.

Accordingly, the amounts reported in 2004 are composed as follows: amounts originating from the period that preceded the transition date are composed of their adjusted to December 2003 shekel amount, 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.

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## AMERICAN ISRAELI PAPER MILLS LIMITED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

### NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (continued):

#### 2) Comparative figures - amounts adjusted to end of 2003

Through December 31, 2003, the Company prepared its financial statements on the basis of historical cost adjusted for the changes in the exchange rate of the dollar, as permitted under Opinion 36 of the Institute of Certified Public Accountants in Israel (hereafter - the Israeli Institute) for companies whose shares are traded on the stock exchange of a foreign country. The Company's shares are traded in the United States on the AMEX.

The comparative figures included in these financial statements are based on the amounts included for the prior reporting periods, as adjusted for the changes in the exchange rate of the dollar, stated at the exchange rate at December 31, 2003 (the exchange rate in effect at the transition date).

The components of the income statements were, for the most part, adjusted as follows: the components relating to transactions carried out during the reported period - sales, purchases, labor

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costs, etc. - were adjusted on the basis of the date in which the transaction was carried out, while those relating to non-monetary balance sheet items (mainly - changes in inventories and depreciation) were adjusted on the same basis as the related balance sheet item. The financing component represents financial income and expenses in real terms and the erosion of balances of monetary items during the year.

The investment in some of the associated companies (whose operations constitute an integral part of the Company's operations) and the company's share in their operating results are recorded on the basis of the adjusted financial statements (in accordance with the provisions of Standard No. 12, as described above) of these companies. As to associated companies whose financial statements were adjusted until December 31, 2003 on the basis of the changes in the CPI, see (4) below.

- 3) The amounts of non-monetary assets do not necessarily represent realization value or current economic value, but only the reported amounts of such assets, as described in (1) above. In these financial statements, the term "cost" signifies cost in reported amounts.
- 4) Associated companies whose financial statements are adjusted on the basis of the changes in the Israeli CPI

For purposes of inclusion on the equity basis, until December 31, 2003, the amounts included in the financial statements of the above associated companies operating independently were treated as follows:

Balance sheet items at the end of the year and the results of operations for the year reflect the amounts presented in the financial statements of such companies. Balance sheet items at the beginning of the year and changes in shareholders' equity items during the year were adjusted on the basis of the changes in the exchange rate of the dollar at the beginning of the year or at the date of each change, respectively, through the end of the year. Any differences resulting from the treatment described above were carried to the adjusted shareholders' equity under a separate item ("currency adjustments in respect of financial statements of associated companies").

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### AMERICAN ISRAELI PAPER MILLS LIMITED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

#### NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (continued):

As from January 1, 2004, no additional differences have been included in respect of said companies, in view of their transition to reporting under Standard 12, as also applied by the Company. The change in this equity item in 2004 is related to a subsidiary of an associated company, which has a currency other than NIS.

#### c. Principles of consolidation:

- 1) The consolidated financial statements include the accounts

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of the Company and its subsidiaries. A list of the main subsidiaries is presented in a schedule to the financial statements.

- 2) Intercompany transactions and balances, as well as intercompany profits on sales which have not yet been realized outside the Group, have been eliminated.

### d. Inventories

Raw materials and supplies, finished goods, purchased products and maintenance and sundry stores are valued at the lower of cost or market (net of processing costs and after deduction of a provision for obsolescence, where appropriate); cost is determined on the moving average basis.

### e. Investments in associated companies:

- 1) The investments in these companies are accounted for by the equity method.
- 2) Profits on intercompany sales, not yet realized outside the Group, have been eliminated according to the percentage of the Company's holding in such companies.
- 3) With effect from the interim financial statements for the 3-month period ended March 31, 2003, the Company reviews whether any events have occurred or changes in circumstances have taken place, which might indicate that there has been an impairment of its investments in associated companies - see h. below.
- 4) The excess of cost of the investment in associated companies over the equity in net assets at time of acquisition ("excess of cost of investment") or the excess of equity in net assets of associated companies at time of acquisition over the cost of their acquisition ("negative excess of cost of investment") represent the amounts attributed to specific assets upon acquisition, at fair value. The excess of cost of investment and the negative excess of cost of investment are presented at their net amount and are amortized over the remaining useful life of the assets. The average rate of amortization is 10%.

### f. Marketable securities

These securities are stated at market prices.

The changes in value of the above securities are carried to financial income or expense.

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AMERICAN ISRAELI PAPER MILLS LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

### NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (continued):

### g. Fixed assets:

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- 1) Fixed assets are stated at cost, net of related investment grants.
- 2) Fixed assets of own manufacture are stated at cost, based on the direct costs with the addition of an appropriate portion of related production costs.
- 3) Borrowing costs in respect of credit applied to finance the construction of the fixed assets - during the period until construction is completed - are charged to cost of such assets.
- 4) The assets are depreciated by the straight-line method on basis of their estimated useful life, as follows:

	Years
Buildings	10-50 (mainly 33)
Machinery and equipment	7-20 (mainly 10 and 20)
Vehicles	5-7 (mainly 7)
Office furniture and equipment (including computers)	3-17 (mainly 4)

### h. Impairment of Assets

In February 2003, Accounting Standard No. 15 of the Israeli Accounting Standard Board (hereafter - IASB) - "Impairment of Assets", became effective. This standard requires a periodic review to evaluate the need for a provision for the impairment of the company's and its subsidiary's non-monetary assets - mainly fixed assets as well as investments in associated companies.

Accordingly, commencing with the interim financial statements for the 3-month period ended March 31, 2003, the Company assesses - at each balance sheet date - whether any events have occurred or changes in circumstances have taken place, which might indicate that there has been an impairment of one or more of the above assets. When such indicators of impairment are present, the Company evaluates whether the carrying value of the asset is recoverable from the cash flows expected from that asset.

The recoverable value of an asset is determined according to the higher of the net selling price of the asset or its value in use to the Company. The value in use is determined according to the present value of anticipated cash flows from the continued use of the asset, including those expected at the time of its future retirement and disposal. When it is not possible to assess whether an impairment provision is required for a particular asset on its own, the need for such a provision is assessed in relation to the recoverable value of the cash generating unit to which that asset belongs.

The adoption of this Standard has not had any effect on the Company and its subsidiaries.

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### NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (continued):

i. Deferred charges

The item represents notes issuance costs, which are amortized over the period of the notes (see note 4a).

j. Deferred income taxes:

- 1) Deferred taxes are computed in respect of differences between the amounts presented in these statements and those taken into account for tax purposes. As to the main factors in respect of which deferred taxes have been included - see note 7f. Deferred tax balances are computed at the tax rate expected to be in effect at time of release to income from the deferred tax accounts. The amount of deferred taxes presented in the income statements reflects changes in the above balances during the reporting years.
- 2) Taxes which would apply in the event of disposal of investments in subsidiaries and associated companies have not been taken into account in computing the deferred taxes, as the Company intends to hold these investments, not to realize them.
- 3) The Group may incur an additional tax liability in the event of intercompany dividend distribution derived from "approved enterprises" profits - see note 7a. No account was taken of this additional tax, since it is the Group's policy not to cause distribution of dividend which would involve an additional tax liability to the Group in the foreseeable future.

k. Revenue recognition

Revenue from sale of products to the local market, net of discounts granted, is recognized upon shipment to the customer (which represents the point at which the title transfers). Revenue from sale of products for export, net of discounts, is recognized as the products are delivered to the customer in the target country.

l. Shipping and handling fees costs

Shipping and handling costs are classified as component of selling and marketing expenses.

m. Allowance for doubtful accounts

The allowance is determined mainly in respect of specific debts doubtful of collection (see note 12b).

n. Derivative financial instruments

Gains or losses from derivatives that are hedging existing assets or liabilities are recognized in income and cash flows statements commensurate with the results from those assets or liabilities.



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### AMERICAN ISRAELI PAPER MILLS LIMITED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

#### NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (continued):

o. Cash equivalents

The Group considers all highly liquid investments, which include short-term bank deposits that are not restricted as to withdrawal or use, the period to maturity of which did not exceed three months at time of deposit, to be cash equivalents.

p. Net income per NIS 1 of par value of shares

Net income per NIS 1 of par value of shares is computed in accordance with Opinion 55 of the Israeli Institute; as to the data used in the per share computation - see note 11.

q. Recently issued pronouncement

In July 2004, the IASB issued Israel Accounting Standard No. 19 - "Taxes on Income", which is based on International Accounting Standard No. 12, that prescribes the accounting treatment (recognition criteria, measurement, presentation and disclosure) required for taxes on income. This accounting standard is to be applied to financial statements covering periods commencing on, or after, January 1, 2005.

For the most part, the provisions of this standard are the same as the accounting principles that are customarily applied at present (see j. above). The adoption of the standard is not expected to have a material effect on the company's financial statements in the forthcoming periods.

#### NOTE 2 - INVESTMENTS IN ASSOCIATED COMPANIES:

- a. The Company has a number of investments in associated companies, which are held either directly or through associated companies. The financial statements of significant associated companies (Mondy Business Paper Hadera Ltd. - formerly Neusiedler Hadera Paper Ltd, NHP - and Hogla-Kimberly Ltd.) are attached to these financial statements.

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### AMERICAN ISRAELI PAPER MILLS LIMITED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

#### NOTE 2 - INVESTMENTS IN ASSOCIATED COMPANIES (continued):

- b. Composed as follows:

December 31  
-----

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	2004	2003
	-----	-----
	NIS in thousands	
Cost:		
Shares	54,241	54,241
Excess of cost of investment - net	2,086	2,086
L e s s - accumulated amortization	(2,624)	(3,068)
Gain on issuance of shares of an associated company to a third party	40,241	40,241
Currency adjustments	(2,807)	(1,122)
Share in profits accumulated since acquisition - net	271,492	246,864
	-----	-----
Long-term loans and capital notes *	362,629	339,242
	69,123	44,637
	-----	-----
	431,752	383,879
	=====	=====

\* Classified by linkage terms, the total amounts of the loans and capital notes are as follows:

	Weighted average interest rate at December 31, 2004 %	December 31 ----- 2004                      2003 ----- NIS in thousands	
Linked to the dollar		8,616	21,897
Linked to the Israeli CPI	0%-6%	11,220	10,553
Loan and unlinked capital note	0%-5%	49,287	12,187
		-----	-----
		69,123	44,637
		=====	=====

As of December 31, 2004, the repayment dates of the balance of the loans and capital notes have not yet been determined.

AMERICAN ISRAELI PAPER MILLS LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 2 - INVESTMENTS IN ASSOCIATED COMPANIES (continued):

c. The changes in the investments during 2004 are as follows:

NIS i  
thousa  
-----

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Balance at beginning of year	383,8
-----	
Changes during the year:	
Share in profits of associated companies - net	25,0
Currency adjustments	(1,6
Classifying long term balance	36,6
Decrease in balance of long-term loans and capital notes - net	(12,1
-----	
Balance at end of year	431,7
=====	

- d. Mondy Business Paper Hadera Ltd. (hereafter - Mondy Hadera; formerly - Neusiedler Hadera Paper Ltd- NHP):

Mondy Hadera is held to the extent of 49.9% by the Company and also by Neusiedler AG (hereafter - Neusiedler), under an agreement dated November 21, 1999. According to said agreement, Mondy Hadera purchased the Group's activities in the field of printing and writing paper, and issued to Neusiedler 50.1% of its shares. As part of the said agreement, Neusiedler was granted an option to sell to the Company its holdings in Mondy Hadera, at a price which is 20% lower than the value (as defined in the agreement). The understanding between the parties is that the option would only be exercised under continued extraordinary circumstances that preclude the operation of Mondy Hadera in Israel. The Company believes that the likelihood of such circumstances is very remote.

- e. Investment in Carmel Container Systems Limited (hereafter - Carmel)

The investment in shares includes, as of December 31, 2004 and 2003, amounts to NIS 32,300,000 and NIS 29,475,000, respectively, which represents a holding of 26.25%. Carmel's shares are traded in the United States on the "AMEX" Stock Exchange. The market value of the Company's holding in these shares as of December 31, 2004 and 2003 is NIS 15,741,000 and NIS 9,656,000, respectively.

In November 2004, Carmel's board of directors decided to take measures to withdraw Carmel's shares from trade on the "AMEX" Stock Exchange in the United States and also to deregister with the SEC. Accordingly, trade in Carmel's shares on the "AMEX" was suspended from November 30, 2004 and the process of deregistering with the SEC is currently being attended to.

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AMERICAN ISRAELI PAPER MILLS LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 2 - INVESTMENTS IN ASSOCIATED COMPANIES (continued):

The Company's management believes that the low market value of these shares is not representative of the economic value, as the trade in Carmel's shares is very weak as described above. At the beginning of 2003, the Company used the services of an outside appraiser in determining the value in use to the Company.

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The Company's management believes, based on the abovementioned and current developments in 2004, that the investment should not be written down.

The financial statements of Carmel are drawn up in accordance with the provisions of Accounting Standard No. 12 of the IASB. Until December 31, 2003, the financial statements have been drawn up on the basis of cost, adjusted for the changes in the general purchasing power of Israeli currency measured on the basis of the Israeli CPI. For purposes of inclusion in the consolidated financial statements up to said date, Carmel's financial statements were adjusted on the basis of the changes in the exchange rate of the dollar.

- f. Investment in T.M.M Integrated Recycling Industries Ltd. (hereafter - T.M.M.)

As of December 31, 2004, the Company's share in T.M.M. (directly and through another associated company) is 41.6%.

The excess of equity in net assets of T.M.M. shares, over the cost of investment therein - amounting to NIS 1,581,000 is amortized over a period of ten years.

As of December 31, 2004 and 2003, the direct investment in the shares of T.M.M is NIS 15,726,000 and NIS 15,759,000, respectively. The market value of these shares as of December 31, 2004 and 2003 is NIS 11,338,000 and NIS 13,713,000, respectively.

The Company's management examined the value of its investment in T.M.M. for impairment which is not temporary in nature. At the beginning of 2003, the Company used the services of an outside appraiser in determining the value in use to the Company.

The Company's management believes, based on the abovementioned and current business developments within T.M.M during 2004, that the investment should not be written down.

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### AMERICAN ISRAELI PAPER MILLS LIMITED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

#### NOTE 3 - FIXED ASSETS:

- a. Composition of assets, grouped by major classifications, and changes therein during 2004, are as follows:

	Cost			
	Balance at beginning of year	Additions during the year	Retirements during the year	Balance at end of year
	-----	-----	-----	-----
	NIS in thousands			
Land and buildings on the land	185,675	3,552		189,227
Machinery and equipment	653,206	25,008	4,461	673,753

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Vehicles	31,860	3,772	5,678	29,954
Office furniture and equipment (including computers)	65,569	2,800	7	68,362
Payments on account of machinery and equipment	17,346	(4,180)		13,166
	-----	-----	-----	-----
	953,656	30,952	10,146	974,462
	=====	=====	=====	=====

	Accumulated depreciation			
	Balance at beginning of year -----	Additions during the year -----	Retirements during the year -----	Balance at end of year -----
	NIS in thousands			
Land and buildings on the land	104,237	3,348		107,585
Machinery and equipment	449,526	19,469	1,168	467,827
Vehicles	22,357	2,786	5,259	19,884
Office furniture and equipment (including computers)	51,895	2,869	4	54,760
Payments on account of machinery and equipment	-----	-----	-----	-----
	628,015	28,472	6,431	650,056
	=====	=====	=====	=====

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AMERICAN ISRAELI PAPER MILLS LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 3 - FIXED ASSETS (continued):

- b. The item is net of investment grants in respect of investments in "approved enterprises" (see notes 7a and 9a).
- c. The Group's real estate is partly owned and partly leased - to the extent of NIS 44.5 million, in respect of which lease fees of approximately NIS 25.8 million have been capitalized. The leasehold rights are for 49-year periods ending in the years 2008 to 2059, with options to extend for an additional 49 years.
- d. As of December 31, 2004 and 2003, the cost of fixed assets includes borrowing costs of NIS 1,007,000 capitalized to the cost of machinery and equipment.
- e. Depreciation expenses amounted to NIS 28,472,000, NIS 28,165,000 and NIS 26,726,000, for the years ended December 31, 2004, 2003 and 2002, respectively.
- f. As to pledges on assets - see note 9a.

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AMERICAN ISRAELI PAPER MILLS LIMITED  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 4 - NOTES AND OTHER LONG-TERM LIABILITIES (continued):

a. Notes

The item represents two series of notes issued to institutional investors as follows:

	December 31		
	-----		
	2004	2003	2002
	-----		
	NIS in thousands		
	-----	-----	-----
	Series II	Series I	Series II
	-----	-----	-----
Balance	201,807	33,340	200,000
L e s s - current maturities		6,648	
	-----	-----	-----
	201,807	26,692	200,000
	=====	=====	=====

(1) Series I - May 1992

The balance of the notes as of December 31, 2004 is redeemable in five installments, due in June of each of the years 2005-2009, each installment amounting to 6.66% of the original par value of the notes, which is NIS 99,819,000, in December 2004 terms; the unpaid balance of the notes bears annual interest of 3.8%, payable each June. The notes - principal and interest - are linked to the Israeli CPI of February 1992.

(2) Series II - December 2003

As of December 31, 2004, the unpaid balance of the notes is payable in 7 annual installments at December of each of the years 2007-2013; The unpaid balance of the notes bears annual interest of 5.65%, payable in annual installments at December of each year. The notes - principal and interest - are linked to the Israeli CPI of November 2003.

b. Other liabilities:

	December 31	
	-----	
	2004	2003
	-----	
	NIS in thousands	
	-----	-----
Capital note to an associated company *	32,770	32,770

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Other liability		2,243
	-----	-----
	32,770	35,013
	=====	=====

\* The capital note is unlinked and interest free. No repayment date has been fixed, but the associated company does not intend to demand the repayment of the capital note before January 1, 2006.

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AMERICAN ISRAELI PAPER MILLS LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 5 - EMPLOYEE RIGHTS UPON RETIREMENT:

- a. Israeli labor laws and agreements require the company and its subsidiaries to pay severance pay to employees dismissed or leaving their employ under certain circumstances, computed on the basis of the number of years of service and, generally, the latest pay rate (one month's pay for each year of service) or a pension upon retirement.

To cover the liability for employee rights upon retirement, pursuant to labor agreements in force and based on salary components which, in management's opinion, create entitlement to severance pay, deposits are made by the Company and its subsidiaries with various provident funds (including pension funds) or insurance policies for the benefit of employees.

The severance pay and pension liability and the amounts funded as above are not reflected in the financial statements, as the pension and severance pay risks have been irrevocably transferred to the pension funds and the insurance companies, as allowed by the Severance Pay Law.

- b. The expenses relating to employee rights upon retirement, which reflect the amounts that were deposited during the reported years with provident funds, pension funds and various insurance policies, are NIS 8,368,000, NIS 8,515,000 and NIS 5,786,000 in 2004, 2003, and 2002, respectively.

NOTE 6 - SHAREHOLDERS' EQUITY:

- a. Share capital

Composed of ordinary registered shares of NIS 0.01 par value, as follows:

	December 31	
	-----	-----
	2004	2003
	-----	-----
Authorized	Issued and paid	

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	-----	-----	-----
Number of shares	20,000,000	3,996,674	3,968,295
	=====	=====	=====
Amount in NIS	200,000	39,967	39,683
	=====	=====	=====

The shares are traded on stock exchanges in Tel-Aviv and in the U.S. The quoted prices per share, as of December 31, 2004 are NIS 238.30 and \$ 55.00 (NIS 236.94), respectively.

b. Employee stock option plans:

1) The 1998 plan for senior officers in the Group

On January 11, 1998, the board of directors approved a stock option plan for senior officers in the Group ("the 1998 plan for senior officers").

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AMERICAN ISRAELI PAPER MILLS LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 6 - SHAREHOLDERS' EQUITY (continued):

In 1998-2000, 155,498 options were granted under the 1998 plan for senior officers.

The number of shares resulted from exercise of the options and the actual exercise price were fixed as follows: Upon the receipt of an exercise request from an option holder, a computation was made of the difference between the quoted price of the Company's shares at the beginning of that trading day and the exercise price; that difference was then multiplied by the number of exercisable options (hereafter - the benefit). The number of shares that the Company actually issued to the option holder was the number of shares the market value of which was equal to the amount of the benefit computed as above. In consideration for the shares, the option holder paid their par value only.

In 2000-2003, 154,000 options were exercised under the 1998 plan for senior officers. 92,832 shares of NIS 0.01 were issued following the exercise. The unexercised balance of 1,498 options granted expired in 2003.

The ordinary shares issued upon exercise of the options conferred upon their holders the same rights as all other ordinary shares, upon issuance.

2) The 2001 plan for senior officers in the Group

On April 2, 2001, the Company's board of directors approved a stock option plan for senior officers in the Group (hereafter - the 2001 plan for senior officers). Under this plan, 194,300 options were allotted on July 5, 2001 without



consideration. Each option is exercisable in purchase of one ordinary share of NIS 0.01 par value of the Company. The options will be exercisable in four equal annual batches. The blocking period of the first batch is two years, commencing on the date of grant; the blocking period of the second batch is three years from the date of grant, and so forth. Each batch is exercisable within two years from the end of the blocking period.

The exercise price of the options granted as above was set at NIS 217.00, linked to the CPI, on the basis of the CPI as of April 2, 2001. The exercise price for each batch is determined as the lesser of the aforementioned exercise price or the average price of the Company's shares as quoted on the Tel-Aviv Stock Exchange (hereafter - the Stock Exchange) during thirty trading days preceding to the effective date of each batch, less 10%. As stipulated by the 2001 plan for senior officers, the exercise price is to be adjusted, following dividend distributions. Accordingly, the exercise price as of December 31, 2004 is NIS 177.37 for the first batch, NIS 68.77 for the second batch, NIS 125.18 for the third batch and NIS 177.37 for the fourth batch.

The quoted price of the Company's shares on the Tel Aviv Stock Exchange close to the time of the board of directors' resolution to grant the options, was NIS 204.00. Prior to the granting of the options, the price was NIS 185.8.

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AMERICAN ISRAELI PAPER MILLS LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 6 - SHAREHOLDERS' EQUITY (continued):

b. Employee stock option plans (continued):

The fair value of each option - computed on the basis of the Black-Scholes option-pricing model - as prescribed by the regulations of the Tel-Aviv Stock Exchange - was approximately NIS 56.69 on the date of grant.

Notwithstanding the above, the number of shares resulting from exercise of the options and the actual exercise price will be determined as follows: when an exercise request is received from an option holder, a computation will be made of the difference between the quoted price of the Company's shares at the beginning of that trading day and the exercise price; that difference is to be multiplied by the number of exercisable options, as of the date of the exercise (hereafter - the benefit). The number of shares that the Company will actually issue to the option holder will be the number of shares the market value of which is equal to the amount of the benefit computed as above. In consideration for the shares, the option holder will pay their par value only.

The ordinary shares issued upon exercise of the options will confer upon their holders the same rights as all other ordinary

shares, upon issuance.

In 2004 and 2003, 55,525 and 1,550 options, respectively, were exercised under the 2001 plan for senior officers, and 24,295 and 227 shares of NIS 0.01, respectively, were issued following the exercise of options, as above. The unexercised balance of the options granted is 137,225.

This plan is designed to be governed by the terms stipulated by Section 102 of the Israeli Income Tax Ordinance. Inter alia, these terms provide that the company will be allowed to claim, as an expense for tax purposes, the amounts credited to the employees as a benefit in respect of shares or options granted under the plan.

The amount allowed as an expense for tax purposes, at the time the employee utilizes such benefit, is limited to the amount of the benefit that is liable to tax as labor income, in the hands of the employee; all being subject to the restrictions specified in Section 102 of the Income Tax Ordinance.

3) The 2001 employee plan

On August 29, 2001, the Company's board of directors approved a stock option plan for employees in the Group, according to a specification (hereafter - the 2001 employee plan). Under this plan, up to 125,000 options will be allotted without consideration. Each option is exercisable in purchase of one ordinary share of NIS 0.01 par value of the Company. The blocking period of the options is two years from the date of grant. Each option is exercisable within three years from the end of the blocking period.

On November 4, 2001, 81,455 options were granted under the 2001 employee plan.

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AMERICAN ISRAELI PAPER MILLS LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 6 - SHAREHOLDERS' EQUITY (continued):

The exercise price of all the options granted as above was set at NIS 160.99, linked to the CPI, on the basis of the CPI as of August 29, 2001. This price represents the average price of the Company's shares as quoted on the Tel-Aviv Stock Exchange during thirty trading days prior to the date of the board of directors' approval, less 10%. As stipulated by the 2001 employee plan, the exercise price has been adjusted, following a dividend distribution and it is NIS 113.57 as of December 31, 2004.

The quoted price of the Company's shares on the Tel Aviv Stock Exchange close to the time of the board of directors' resolution to grant the options, was NIS 171.20. Prior to the granting of the options, the price was NIS 138.80.

The fair value of each option - computed on the basis of the Black-Scholes option-pricing model - as prescribed by the

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regulations of the Tel-Aviv Stock Exchange - was approximately NIS 64.11 on the date of grant.

Notwithstanding the above, the number of shares resulting from exercise of the options and the actual exercise price will be fixed as follows: when an exercise request is received from an option holder, a computation will be made of the difference between the quoted price of the Company's shares at the beginning of that trading day and the exercise price; that difference is to be multiplied by the number of exercisable options, as of the date of the exercise (hereafter - the benefit). The number of shares that the Company will actually issue to the option holder will be the number of shares the market value of which is equal to the amount of the benefit computed as above. In consideration for the shares, the option holder will pay their par value only.

The ordinary shares issued upon exercise of the options will confer upon their holders the same rights as all other ordinary shares, upon issuance.

In 2004 and 2003, 8,615 and 57,962 options, respectively, were exercised under the 2001 employee plan. 4,084 and 20,665 shares of NIS 0.01, respectively, were issued following the exercise of options, as above. The unexercised balance of the options granted is 14,878.

This plan is designed to be governed by the terms stipulated by Section 102 of the Israeli Income Tax Ordinance. Inter alia, these terms provide that the company will be allowed to claim, as an expense for tax purposes, the amounts credited to the employees as a benefit in respect of shares or options granted under the plan.

The amount allowed as an expense for tax purposes, at the time the employee utilizes such benefit, is limited to the amount of the benefit that is liable to tax as labor income, in the hands of the employee; all being subject to the restrictions specified in Section 102 of the Income Tax Ordinance.

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### AMERICAN ISRAELI PAPER MILLS LIMITED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

#### NOTE 7 - TAXES ON INCOME:

- a. Tax benefits under the Law for the Encouragement of Capital Investments, 1959 (hereafter - the law)

Under the law, by virtue of the "approved enterprise" status granted to certain of their production facilities, certain subsidiaries were entitled to various tax benefits (mainly reduced tax rates) until 2003.

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During the period of benefits - mainly 7 years commencing in the first year in which the companies earn taxable income from the approved enterprises, provided the maximum period to which it is restricted by law has not elapsed - reduced tax rates or exemption from tax apply, as follows:

- 1) Corporate tax rate of 25%, instead of the regular tax rate (see d. below).
- 2) Tax exemption on income from certain approved enterprises in respect of which the companies have elected the "alternative benefits" (involving waiver of government guaranteed loans); the length of the exemption period is 4 years, after which the income from these enterprises is taxable at the rate of 25% for 3 years.

The part of the taxable income which is entitled to the tax benefits is determined on the basis of the ratio of the turnover attributed to the "approved enterprise" to the total turnover of these companies, taking into account the ratio of the "approved enterprise" assets to total assets of these companies. The turnover that is attributed to the "approved enterprise" is generally computed on the basis of the ratio of the increase in turnover to the "basic" turnover stipulated in the instrument of approval.

The period of benefits in respect of the "approved enterprises" of these companies expired at the end of 2003.

The entitlement to the above benefits is conditional upon the companies' fulfilling the conditions stipulated by the law, regulations published thereunder and the instruments of approval for the specific investments in "approved enterprises". In the event of failure to comply with these conditions, the benefits may be cancelled and the companies may be required to refund the amount of the benefits, in whole or in part, with the addition of linkage differences to the CPI and interest.

- b. Measurement of results for tax purposes under the Income Tax (Inflationary Adjustments) Law, 1985 (hereafter - the inflationary adjustments law)

Under the inflationary adjustments law, results for tax purposes are measured in real terms, having regard to the changes in the Israeli CPI. The Israeli companies in the Group are taxed under this law.

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### AMERICAN ISRAELI PAPER MILLS LIMITED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

#### NOTE 7 - TAXES ON INCOME (continued):

- c. The Law for the Encouragement of Industry (Taxation), 1969  
The Company and certain subsidiaries are "industrial companies"

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as defined by this law. These companies claimed depreciation at accelerated rates on equipment used in industrial activity as stipulated by regulations published under the inflationary adjustments law.

The Company also files consolidated tax returns with certain subsidiaries as permitted under this law.

- d. Tax rates applicable to income not derived from "approved enterprises"

The income of the Company and its Israeli subsidiaries (other than income from "approved enterprises", see a. below) is taxed at the regular rate. Through to December 31, 2003, the corporate tax was 36%. In July 2004, an amendment to the Income Tax Ordinance was enacted. One of the provisions of this amendment is that the corporate tax rate is to be gradually reduced from 36% to 30%, in the following manner: the rate for 2004 will be 35%, in 2005 - 34%, in 2006 - 32%, and in 2007 and thereafter - 30%. The effect of the change in the tax rates in the coming years on the deferred tax balances on the effective date of the amendment to the law, is included under "taxes on income" in the statements of income (loss) - see g (1) below.

- e. Carryforward tax losses

Carryforward tax losses are NIS 20,399,000 and NIS 14,002,000 as of December 31, 2004 and 2003, respectively. Under the inflationary adjustments law, carryforward losses are linked to the Israeli CPI, and may be utilized indefinitely.

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### AMERICAN ISRAELI PAPER MILLS LIMITED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

#### NOTE 7 - TAXES ON INCOME (continued):

- f. Deferred income taxes

The composition of the deferred taxes, and the changes therein during 2004 and 2003, are as follows:

	Among non-current assets (1) -----	Among current assets (2) -----	Among non-current liability (3) -----
	NIS in thousands		
Balance at January 1, 2003	(10,948)		58,266
Changes in 2003:			
Reclassification	3,885	(3,885)	
Amounts carried to income	(64)		3,535
	-----	-----	-----
Balance at December 31, 2003	(7,127)	(3,885)	61,801
Changes in 2004:			

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Amounts carried to income	1,769	(2,626)	(9,239)
	-----	-----	-----
Balance at December 31, 2004	(5,358)	(6,511)	52,562
	=====	=====	=====

(1) In respect of inventories, provisions for doubtful accounts, vacation and recreation pay, and carry-forward tax losses.

(2) In respect of carryforward tax losses.

(3) Mainly in respect of depreciable fixed assets.

The deferred taxes are computed at the rate of 30%-34%.

g. Taxes on income included in the income statements:

1) As follows:

	2004	2003
	-----	-----
	NIS in thousands	
For the reported year:		
Current	13,248	4,235
Deferred, see f. above:		
In respect of changes to tax rates, see d. above	(5,824)	
In respect of the reporting period	(4,272)	3,471
	-----	-----
	3,152	7,706
For previous years - Current		
	-----	-----
	3,152	7,706
	=====	=====

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AMERICAN ISRAELI PAPER MILLS LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 7 - TAXES ON INCOME (continued):

2) Following is a reconciliation of the "theoretical" tax expense, assuming all income is taxed at the regular rate, as stated in d. above, and the actual tax expense:

	2004		2003	
	-----		-----	
	%	NIS in thousands	%	NIS in thousands

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	-----	-----	-----	-----
Income before taxes on income, as reported in the statements of income	100.0	40,812	100.0	32,204
	=====	=====	=====	=====
Theoretical tax on the above amount	35.0	14,284	36.0	11,593
Tax benefits arising from reduced tax rate for approved enterprises			(1.5)	(487)
	-----	-----	-----	-----
	35.0	14,284	34.5	11,106
Decrease in taxes resulting from computation of deferred taxes at a rate which is different from the theoretical rate	(4.3)	(1,762)		
Tax benefit resulting from changes in tax rates, see d. above	(14.3)	(5,824)		
Tax deduction in respect of options exercised by employees according to section 102 of the Israeli Income Tax Ordinance	(10.3)	(4,221)	(5.0)	(1,607)
Other - net	1.6	675	(5.6)	(1,793)
	-----	-----	-----	-----
Taxes on income for the reported year	7.7	3,152	23.9	7,706
	=====	=====	=====	=====

h. Tax assessments

The Company and most of its subsidiaries have received final tax assessments through the year ended December 31, 2000.

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AMERICAN ISRAELI PAPER MILLS LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 8 - LINKAGE TERMS OF MONETARY BALANCES:

a. As follows:

	December 31, 2004	
	-----	-----
	In, or linked to, foreign currency (mainly dollar)	Linked to the Israeli CPI
	-----	-----
		NIS in thousands
Assets:		
Current assets:		
Cash and cash equivalents	4,531	
Short-term investments		45,539
Receivables	43,600	1,799
Investments in associated companies - long-term loans and capital notes	8,616	11,220
	-----	-----

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	56,747	58,558
	=====	=====
Liabilities:		
Current liabilities:		
Short-term credit from banks	2,238	
Accounts payables and accruals	10,100	1,013
Long-term liabilities (including current maturities):		
Loans from banks		
Notes		235,147
Other liabilities		
	-----	-----
	12,338	236,160
	=====	=====
		December 31, 20
		-----
	In, or linked to, foreign currency (mainly dollar)	Linked to the Israeli CPI
	-----	-----
		NIS in thousands
Assets:		
Current assets:		
Cash and cash equivalents	8,561	
Short-term investments		
Receivables	48,457	215
Investments in associated companies - long-term loans and capital notes	21,897	10,553
	-----	-----
	78,915	10,768
	=====	=====
Liabilities:		
Current liabilities:		
Short-term credit from banks		
Accounts payables and accruals	11,579	
Long-term liabilities (including current maturities):		
Loans from banks		372
Notes		239,629
Other liabilities	2,243	
	-----	-----
	13,822	240,001
	=====	=====

As to exposures relating to fluctuations in foreign currency exchange rates and the use of derivatives for hedging purposes - see note 12a.

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AMERICAN ISRAELI PAPER MILLS LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 8 - LINKAGE TERMS OF MONETARY BALANCES (continued):

b. Data regarding the exchange rate and the Israeli CPI:



	Exchange rate of one dollar ----- NIS	CPI* ----- Points
At end of year:		
2004	4.308	180.7
2003	4.379	178.6
2002	4.737	182.0
Change in the year:		
2004	(1.6%)	1.2%
2003	(7.6%)	(1.9%)
2002	7.3%	6.5%

\* Based on the index for the month ending on each balance sheet date, on the basis of 1993 average = 100.

NOTE 9 - COMMITMENTS, CONTINGENT LIABILITIES AND LIABILITIES SECURED BY PLEDGES:

a. In respect of investment grants

Under the Law for the Encouragement of Capital Investments, 1959, certain subsidiaries and an associated company have received investment grants from the State of Israel. In the event of failure to comply with the terms attached to the receipt of the grants, the companies may be required to refund the amount of the grants, in whole or in part, with linkage differences and interest from the date of receipt.

The abovementioned subsidiaries have registered floating charges on all their assets in favor of the State of Israel as security for compliance with the terms of the investment grants received. In respect of the grant received by the associated company, the Company has provided a guarantee, with another associated company, for the repayment of the grant. As of December 31, 2004, the guarantee amounts to NIS 181,000.

b. In 1996, an associated company received a grant amounting to NIS 2,067,000 from the Fund for Preparation for Exposure of the Ministry of Industry and Trade. With respect to this grant, the Company has provided a bank guarantee of NIS 2,036,000 in favor of the State of Israel.

c. The Company has provided guarantees of NIS 2,154,000 in favor of an associated company, in connection with the latter's participation in a tender. If the associated company does not win the tender, the guarantee will become null and void.

d. A subsidiary has provided a guarantee of NIS 1,291,000 to a bank in respect of a loan extended to an associated company.

e. A subsidiary provided guarantees to various entities, in connection with tenders, in the aggregate amount of approximately NIS 1,700,000.

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AMERICAN ISRAELI PAPER MILLS LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 9 - COMMITMENTS, CONTINGENT LIABILITIES AND LIABILITIES SECURED BY PLEDGES  
(continued):

- f. On May 7, 2001, the Company's board of directors resolved to carry out a plan, which was approved by the shareholders' meeting, to remunerate the Company's chairman of the board of directors. According to the plan, a remuneration will be granted, equal to the increase in the value of 50,000 shares of the Company in the period from May 7, 2001 (share price - NIS 194.37, linked to the terms of the plan) to May 7, 2008. The remuneration will be spread over the period commencing two years from the resolution of the board of directors, until the end of seven years from said resolution. In 2004, one quarter of the remuneration was exercised. As of December 31, 2004, another quarter is exercisable. A liability was included in the financial statements in respect of the above plan, under current liabilities.
- g. In accordance with the Companies Law, 1999, in 2004, the Company issued new letters of indemnity to its officers, pursuant to which the Company undertakes to indemnify the officers for any liability or expense, for which indemnification may be paid under the law, that may be incurred by the officers in connection with actions performed by them as part of their duties as officers in the Company, which are directly or indirectly related to the events specified in the addendum to the letters of indemnity, provided that the total amount of indemnification payable to the officers, shall not exceed 25% of the Company's shareholders' equity as per its latest financial statements published prior to the actual indemnification. The liability of officers in connection with the performance of their duties, as above, is partly covered by an insurance policy.

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AMERICAN ISRAELI PAPER MILLS LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 10 - SUPPLEMENTARY FINANCIAL

STATEMENT INFORMATION:

Balance sheets:

Weighted average  
interest rate  
at December 31,  
2004  
-----

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- a. Short-term investments: 4.0%
- Short term deposit - linked to the CPI
  - Short-term deposit - unlinked
  - Marketable securities
- b. Receivables:
- 1) Trade:
    - Open accounts
    - Checks collectible
- The item is:  
Net of allowance for doubtful accounts
- Includes associated companies
- 2) Other:
    - Employees and employee institutions
    - Associated companies
    - Prepaid expenses
    - Advances to suppliers
    - Deferred income taxes, see note 7f
    - Income tax authority
    - Interest receivable
    - Sundry
- c. Inventories:
- For industrial activities:
    - Finished goods
    - Raw materials and supplies
- For commercial activities - purchased products
- Maintenance and sundry stores
- d. Credit from banks:
- Short-term credit - unlinked 4.5%
  - Short-term credit - Swiss franc 3.2%
  - Current maturities of long-term  
Loans

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NOTE 10 - SUPPLEMENTARY FINANCIAL STATEMENT INFORMATION (continued):

e. Accounts payable and accruals - other:

	December 31	
	2004	2003
	NIS in thousands	
Payroll and related expenses	34,904	37,324
Institutions in respect of employees	10,551	12,944
Customs and value added tax authorities	3,850	728
Associated company	511	521
Accrued interest	1,544	2,127
Accrued expenses	7,903	7,825
Sundry	7,092	11,541
	66,355	73,010
	=====	=====

Statements of income:

	2004	2003	2002
	NIS in thousands		
f. Sales - net (1):			
Industrial activities (2)	363,489	326,825	310,628
Commercial activities	119,365	138,267	145,147
	482,854	465,092	455,775
	=====	=====	=====
(1) Including sales to associated companies	121,987	115,505	104,864
	=====	=====	=====
(2) Including sales to export	42,232	44,175	40,645
	=====	=====	=====
g. Cost of sales:			
Industrial activities:			
Materials consumed	83,533	72,292	61,649
Payroll and related expenses	91,468	85,419	78,903
Depreciation	24,537	22,739	21,182
Other manufacturing costs	82,991	80,709	77,765
Decrease (increase) in inventory of finished goods	3,135	(1,651)	12,585
	285,664	259,508	252,084
Commercial activities - cost of products sold	90,240	102,677	111,687
	375,904	362,185	363,771
	=====	=====	=====

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Including purchases from associated Companies	22,793	26,374	29,423
--	--------	--------	--------

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AMERICAN ISRAELI PAPER MILLS LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 10 - SUPPLEMENTARY FINANCIAL STATEMENT INFORMATION (continued):

	2004 -----	2003 -----
	NIS in thous	
h. Selling, marketing, administrative and general expenses:		
Selling and marketing:		
Payroll and related expenses	14,311	15,225
Packaging, transport and shipping	6,458	5,719
Commissions	2,467	2,733
Depreciation	1,159	1,595
Other	6,200	6,052
	-----	-----
	30,595	31,324
	=====	=====
Administrative and general:		
Payroll and related expenses	36,649	36,360
Office supplies, rent and maintenance	1,521	1,938
Professional fees	1,029	*1,663
Depreciation	2,776	2,814
Doubtful accounts and bad debts	3,102	944
Other	1,735	*4,681
	-----	-----
	46,812	48,400
L e s s - rent and participation from associated companies	24,387	23,401
	-----	-----
	22,425	24,999
	=====	=====
		* Reclassified
i. Financial income (expenses) - net*: Expenses:		
In respect of long-term loans - net	26	1,607
In respect of notes - including amortization of deferred charges	15,188	5,031
Erosion of operating monetary balances, net of related hedges		
In respect of short-term balances - net (2002 -net of borrowing costs capitalized to the cost of fixed assets)	6,547	16,917
	-----	-----
	21,761	23,555
	-----	-----

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Income:		
In respect of long-term loans - net		
In respect of increase in value of operating monetary balances, net of related hedges	1,901	**7,429
In respect of short-term balances - net	6,742	** 137
	-----	-----
	8,643	7,566
	-----	-----
	(13,118)	(15,989)
	=====	=====
* Including financial income (expenses) in respect of loans to associated companies	721	(1,376)
	=====	=====

\*\* Reclassified

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AMERICAN ISRAELI PAPER MILLS LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 10 - SUPPLEMENTARY FINANCIAL STATEMENT INFORMATION (continued):

	2003	2002
	-----	-----
	NIS in thousands	
j. Other income (expenses):		
From the sale of apartments (1)	1,609	
From termination of an activity and disposal of assets(2)		(2,942)
	-----	-----
	1,609	(2,942)
	=====	=====

- 1) In 2003, the Company sold apartments that it previously held for the use of its employees.
- 2) In 2002, the Company terminated operations at some of its sites, as follows:
  - a) At the Molett site in Nahariya, the operation of the old household paper machine was terminated, following the introduction of a new tissue machine by Hogla-Kimberly Ltd., an associated company. Subsequently, the old paper machine was sold to a third party (overseas).
  - b) In order to comply with the requirements of the Ministry of Environment, the operation of the old paper machines at the Shafir site in Tel-Aviv were terminated. The termination included dismissal of employees, sale of maintenance stores, sale of the machines to a third party (overseas) and other related costs (including closing inventories).
  - c) The Company sold real estate that it owned in Ashdod.

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The effects of the restructuring resulting from the termination of the operations are as follows:

	2002
	-----
	NIS in thousands
	-----
Severance pay expenses	(2,334)
Other expenses, net of sale proceeds	(4,475)
Gain on sale of real estate in Ashdod	3,867
	-----
	(2,942)
	=====

NOTE 11 - NET INCOME PER NIS 1 OF PAR VALUE OF SHARES:

- a. The weighted average par value of shares used in computation of per share data is as follows:

	NIS
	---
Year ended December 31:	
2004	40,640
====	=====
2003	40,197
====	=====
2002	39,557
====	=====

- b. In the reported years, plans for granting stock options to employees in the Group were taken into account in computing per share data, having regard to the quoted price of the Company's share at the end of each year.

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AMERICAN ISRAELI PAPER MILLS LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 12 - FINANCIAL INSTRUMENTS AND RISK MANAGEMENT:

- a. Derivative financial instruments

The Company has limited involvement with derivative financial instruments. The Company uses these instruments as hedges. The Company utilizes derivatives, mainly forward exchange contracts and currency options, to protect its cash flows in respect of existing assets and liabilities denominated in currencies other than the functional currency of the Company or that are linked to the CPI. As the counter-parties to these derivatives are Israeli banks, the Company considers the inherent credit risks remote.

In January 2004, the Company entered into a forward transaction for a period of one year, in order to hedge an amount of NIS 200 million against increases in the Israeli CPI.

At the end of 2004, the Company entered into a forward transaction for a period of one year, in order to hedge an amount

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of NIS 200 million against increases in the CPI, following the termination of the aforementioned transaction in January 2005.

### b. Credit risks

The Company and its subsidiaries' cash and cash equivalents and the short-term deposit as of December 31, 2004 are deposited mainly with major Israeli banks. The Company and its subsidiaries considers the credit risks in respect of these balances to be remote.

Most of these companies sales are made in Israel, to a large number of customers. The exposure to credit risks relating to trade receivables is limited due to the relatively large number of customers. The Group performs ongoing credit evaluations of its customers to determine the required amount of allowance for doubtful accounts. An appropriate allowance for doubtful accounts is included in the financial statements.

### c. Fair value of financial instruments

The fair value of the financial instruments included in working capital of the Group is usually identical or close to their carrying value. The fair value of loans and other liabilities also approximates the carrying value, since they bear interest at rates close to the prevailing market rates, except as described below.

The Company does not disclose the fair value of long-term loans and capital notes included under investments in associated companies as of December 31, 2004, aggregating NIS 69,123,000 (see note 2b) and of a capital note to an associated company in the amount of NIS 32,770,000 (see note 4b.), since their value cannot be reliably determined so long as they have no repayment dates.

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## AMERICAN ISRAELI PAPER MILLS LIMITED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

### NOTE 13 - INTERESTED PARTIES - TRANSACTIONS AND BALANCES:

#### a. Transactions:

#### 1) Income (expenses):

	2004	2003	2002
	-----	-----	-----
	NIS in thousands		
Sales	45,278	38,715	36,030
	=====	=====	=====
Costs and expenses	(9,247)	(7,009)	(6,038)
	=====	=====	=====

The amounts presented above represent transactions that the Company carried out in the ordinary course of business with interested parties (companies which are held by the Company's



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principal shareholder), at terms and prices similar to those applicable to non-affiliated customers and suppliers.

2) Benefits to interested parties:

	2004 -----	2003 -----	2002 -----
Payroll to interested parties employed By the Company - NIS in thousands	*3,300 =====	*3,364 =====	2,000 =====
Number of people to whom the benefits relate	2 =====	2 =====	1 =====
Remuneration of directors who are not employed by the Company - NIS in thousands	528 =====	444 =====	324 =====
Number of people to whom the benefits relate	13 =====	13 =====	9 =====

\* In 2004 and 2003, the amounts include the salary of the CEO who was appointed in April 2003 and ended his office in April 2004, in addition to the salary of the Chairman of the Board of Directors (who served earlier as the CEO). The amount for 2004 includes a quarter of the remuneration to the Chairman of the Board of Directors, see note 9f.

3) In 2003, an interested party employed by the Company exercised 15,999 options granted to him under the 1998 plan for senior employees. 8,529 shares of NIS 0.01 par value have been issued at par against the exercise of said options.

4) As to the plan for the remuneration of the Company's Chairman of the Board of Directors - see note 9f.

b. Balances with interested parties:

	December 31	
	2004 -----	2003 -----
	NIS in thousands	
Accounts receivable - commercial activity*	13,378 =====	10,440 =====
Accounts payables and accruals	3,563 =====	2,430 =====

\* There were no significant changes in the balance during the year.

AMERICAN ISRAELI PAPER MILLS LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

## NOTE 14 - SEGMENT INFORMATION:

## a. Activities of the Company and its subsidiaries:

- 1) Manufacturing and marketing of packaging paper, including collection and recycling of paper waste. The manufacturing of paper relies mainly on paper waste as raw material.
- 2) Marketing of office supplies and paper, mainly to institutions.

Most of the Group's sales are to the local market (Israel) and most of its assets are located in Israel.

AMERICAN ISRAELI PAPER MILLS LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

## NOTE 14 - SEGMENT INFORMATION (continued):

## b. Business segment data:

	Paper and recycling			Market
	2004	2003	2002	2004
	-----			
	-----	-----	-----	-----
	NIS in thousands			
Sales - net(1)	367,391	332,124	314,636	115,463
Income (loss) from ordinary operations	58,496	46,282	37,488	(4,566)
Financial expenses, net				
Other income (expenses)				
Income before taxes on income				
Segment assets (at end of year)	494,194	497,811	482,833	56,707
Unallocated assets (at end of year) (2)				
Consolidated total assets (at end of year)				
Segment liabilities (at end of year)	66,564	58,906	66,325	20,992
Unallocated liabilities (at end of year)				
Consolidated total liabilities (at end of year)				
Depreciation and amortization	26,671	25,523	24,422	1,962

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	T o t a l		
	2004	2003	2002
	----- N I S i n t h o u s a n d s -----		
Sales - net(1)	482,854	465,092	455,775
	=====	=====	=====
Income (loss) from ordinary operations	53,930	46,584	36,455
Financial expenses, net	13,118	15,989	2,988
Other income (expenses)		1,609	(2,942)
	-----	-----	-----
Income before taxes on income	40,812	32,204	30,525
Segment assets (at end of year)	550,901	557,291	548,067
Unallocated assets (at end of year) (2)	611,486	695,983	504,056
	-----	-----	-----
Consolidated total assets (at end of year)	1,162,387	1,253,274	1,052,123
	=====	=====	=====
Segment liabilities (at end of year)	87,566	84,602	99,255
Unallocated liabilities (at end of year)	499,518	554,442	301,918
	-----	-----	-----
Consolidated total liabilities (at end of year)	587,074	639,044	401,173
	=====	=====	=====
Depreciation and amortization	28,633	28,247	26,809
	=====	=====	=====

- (1) Represents sales to external customers.
- (2) Including investments in associated companies.

-----  
-----  
-----

AMERICAN ISRAELI PAPER MILLS LIMITED  
Details of Subsidiaries and Associated Companies  
At December 31, 2004

Percent  
indirect  
conf

Main subsidiaries:  
Amnir Recycling Industries Limited

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Graffiti Office Supplies and Paper Marketing Ltd.  
Attar Marketing Office Supplies Ltd.  
American Israeli Paper Mills Paper Industry (1995) Ltd.

### Main associated companies:

Hogla-Kimberly Ltd.

Subsidiaries of Hogla-Kimberly Ltd.:

Hogla-Kimberly Marketing Limited

Molett Marketing Limited

Shikma For Personal Comfort Ltd.

Ovisan Sihhi Bez Sanai Ve Ticavet A.S.

Hogla-Kimberly Holdings A.S.

H-K Overseas (Holland) B.V.

Mondy Business Paper Hadera Ltd.

Subsidiaries of Mondy Business Paper Hadera Ltd.:

Grafinir Paper Marketing Ltd.

Yavnir (1999) Ltd.

Mondy Business Paper Hadera Marketing Ltd.

Mitrani Paper Marketing 2000 (1998) Ltd.

Carmel Container Systems Limited

C.D. Packaging Systems Limited\*

Barthelemi Holdings Ltd.

T.M.M. Integrated Recycling Industries Ltd.\*\*

\* C.D. Packaging Systems Limited is partly held through Carmel Container Systems Limited (an associated company); the holding in voting shares of C.D. Packaging Systems Limited is 63.05%.

\*\* T.M.M Integrated Recycling Industries Ltd. is partly held directly and partly through Barthelemi Holdings Ltd.

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[GRAPHIC OMITTED]

Enclosed please find the financial reports of the following associated companies:

- Mondi Business Paper Hadera Ltd.
- Hogla-Kimberly Ltd.

The financial report of the following associated companies are not included:

- Carmel Containers Systems Ltd., according to section 44(c) of the Securities (Periodic and Immediate Reports) Regulations.

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- TMM Integrated Recycling Industries Ltd., a reporting corporation.

EXHIBIT 4

MONDI BUSINESS PAPER HADERA LTD.  
(FORMERLY, NEUSIEDLER HADERA PAPER LTD.)  
FINANCIAL STATEMENTS  
AS OF DECEMBER 31, 2004

MONDI BUSINESS PAPER HADERA LTD.  
(FORMERLY, NEUSIEDLER HADERA PAPER LTD.)  
FINANCIAL STATEMENTS  
AS OF DECEMBER 31, 2004

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Independent Auditors' Report  
to the Shareholders of  
Mondi Business Paper Hadera Ltd.  
(formerly, Neusiedler Hadera Paper Ltd.)

We have audited the accompanying balance sheet of Mondi Business Paper Hadera Ltd. ("the Company") as of December 31, 2004, and the consolidated balance sheet

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as of that date, and the related statements of operations, changes in shareholders' equity and cash flows - of the Company and on a consolidated basis - for the year then ended. These financial statements are the responsibility of the Company's Board of Directors and management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of the Company and on a consolidated basis as of December 31, 2003 and for each of the two years in the period then ended were audited by other auditors whose report, dated March 10, 2004, expressed an unqualified opinion on those financial statements.

We conducted our audit in accordance with standards of the Public Company Accounting Oversight Board (United States) and with generally accepted auditing standards in Israel, including those prescribed by the Israeli Auditors' Regulations (Mode of Performance), 1973. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by the Board of Directors and management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position - of the Company and on a consolidated basis - as of December 31, 2004 and the results of operations, changes in shareholders' equity and cash flows - of the Company and on a consolidated basis - for the year then ended, in accordance with generally accepted accounting principles in Israel. In addition, in our opinion, the financial statements referred to above are prepared in accordance with the Israeli Securities Regulations (Preparation of Annual Financial Statements), 1993.

Accounting principles generally accepted in Israel vary in certain significant respects from accounting principles generally accepted in the United States of America. The application of the latter would have affected the determination of the financial position and results of operations as of the dates and for the years presented.

As explained in Note 2A, the financial statements as of dates and for reporting period commencing January 1, 2004, are presented at reported amounts, in accordance with accounting standards of the Israeli Accounting Standards Board. The financial statements as of dates prior to January 1, 2004 and for reporting periods ended through December 31, 2003, have been prepared on the basis of historical cost adjusted for changes in the exchange rate of the U.S. dollar in relation to the NIS, in accordance with pronouncements of the Institute of Certified Public Accountants in Israel.

Brightman Almagor & Co.  
Certified Public Accountants  
A Member Firm of Deloitte Touche Tohmatsu

Tel Aviv, February 23, 2005

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MONDI BUSINESS PAPER HADERA LTD.  
(FORMERLY, NEUSIEDLER HADERA PAPER LTD.)  
BALANCE SHEETS  
(NIS in thousands)

		Consolidated	
		December 31,	
		2 0 0 4	2 0 0 3
	Note	Reported Amounts (1)	Adjusted Amounts (2)
	---	-----	-----
<b>Current Assets</b>			
Cash and cash equivalents	3	10,804	31,678
Trade receivables	4	157,815	147,748
American Israeli Paper Mills Group, net		-	-
Other receivables	5	7,580	11,296
Inventories	6	90,391	89,231
		-----	-----
		266,590	279,953
		-----	-----
<b>Long-Term Investments</b>			
Investments in Subsidiaries	7	-	-
		-----	-----
<b>Fixed Assets</b>			
Cost	8	149,083	132,692
Less - accumulated depreciation		33,345	25,381
		-----	-----
		115,738	107,311
		-----	-----
<b>Other Assets - Goodwill</b>			
	7B	3,800	4,423
		-----	-----
		386,128	391,687
		=====	=====
<b>Current Liabilities</b>			
Current maturities of long-term			
bank loans	11	15,125	15,108
Trade payables	9	104,661	104,097
American Israeli Paper Mills Group, net		65,033	(*) 48,786
Subsidiaries		-	-
Other payables and accrued expenses	10	23,132	(*) 16,864
		-----	-----
		207,951	184,855
		-----	-----
<b>Long-Term Liabilities</b>			
Long-term bank loans	11	36,248	51,725
Capital notes to shareholders	12	17,233	43,790
Deferred taxes	21	25,422	29,247
Accrued severance pay, net	13	87	145
		-----	-----
		78,990	124,907
		-----	-----
<b>Commitments and Contingent Liabilities</b>			
	14		

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Shareholders' Equity			
Share capital	15	1	1
Premium		43,352	43,352
Retained earnings		55,834	38,572
		-----	-----
		99,187	81,925
		-----	-----
		386,128	391,687
		=====	=====

- (\*) Reclassified.  
(1) See Note 2A.  
(2) Adjusted for changes in the exchange rate of the U.S. dollar as of December 31, 2003.

-----	-----	-----
E. Amar	A. Solel	Y. Yerushalmi
Chief Financial Officer	General Manager	Vice Chairman of the Board of Directors

Approval date of the financial statements: February 23, 2005.

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

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MONDI BUSINESS PAPER HADERA LTD.  
(FORMERLY, NEUSIEDLER HADERA PAPER LTD.)  
STATEMENTS OF OPERATIONS  
(NIS in thousands, except per share data)

	Note	Consolidated			2 0 0 0
		Year ended December 31,			
		2 0 0 4	2 0 0 3	2 0 0 2	
		Reported Amounts (1)	Adjusted Amounts (2)	Adjusted Amounts (2)	Report Amounts
Net sales	16	686,094	(*) 640,020	(*) 574,227	482,69
Cost of sales	17	605,738	556,890	(*) 491,712	416,50
Gross profit		80,356	83,130	82,515	66,19
Selling expenses	18	46,135	42,892	(*) 40,731	34,60
General and administrative expenses	19	7,803	(*) 8,425	(*) 10,212	6,44
Operating profit		26,418	31,813	31,572	25,14
Financing expenses, net	20	(8,438)	(*) (2,561)	(*) (3,852)	(7,64



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Other income (expenses), net	100	(*)	(215)	(*)	(109)	4
	-----		-----		-----	-----
Income before income taxes	18,080		29,037		27,611	17,55
Income taxes	21		818		10,518	11,534
	-----		-----		-----	-----
Income after income taxes	17,262		18,519		16,077	17,19
Equity in net earnings (losses) of Subsidiaries	-		-		-	7
	-----		-----		-----	-----
Net income for the year	17,262		18,519		16,077	17,26
	=====		=====		=====	=====
Earnings per share (in NIS)	17,262		18,519		16,077	17,26
	=====		=====		=====	=====
Number of shares used In computation	1,000		1,000		1,000	1,00
	=====		=====		=====	=====

(\*) Reclassified.

(1) See Note 2A.

(2) Adjusted for changes in the exchange rate of the U.S. dollar as of December 31, 2003.

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

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MONDI BUSINESS PAPER HADERA LTD.  
(FORMERLY, NEUSIEDLER HADERA PAPER LTD.)  
STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY  
(NIS in thousands)

	Share capital	Premium	Retain earnin
	-----	-----	-----
Balance - January 1, 2002 (Adjusted Amounts (2))	1	43,352	3,97
Changes during 2002:			
Net income for the year	-	-	16,07
	-----	-----	-----
Balance - December 31, 2002 (Adjusted Amounts (2))	1	43,352	20,05
Changes during 2003:			
Net income for the year	-	-	18,51
	-----	-----	-----

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Balance - December 31, 2003 (Adjusted Amounts (2))	1	43,352	38,57
Changes during 2004:			
Net income for the year	-	-	17,26
Balance - December 31, 2004 (Reported Amounts (1))	1	43,352	55,83

(1) See Note 2A.

(2) Adjusted for changes in the exchange rate of the U.S. dollar as of December 31, 2003.

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

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MONDI BUSINESS PAPER HADERA LTD.  
(FORMERLY, NEUSIEDLER HADERA PAPER LTD.)  
STATEMENTS OF CASH FLOWS  
(NIS in thousands)

	Consolidated			
	Year ended December 31,			
	2 0 0 4	2 0 0 3	2 0 0 2	
Reported Amounts (1)	Adjusted Amounts (2)	Adjusted Amounts (2)	Reported Amounts (1)	
Cash flows - operating activities				
Net income for the year	17,262	18,519	16,077	17,262
Adjustments to reconcile net income to net cash provided by operating activities (Appendix A)	20,295	37,698	31,659	30,855
Net cash provided by operating activities	37,557	56,217	47,736	48,117
Cash flows - investing activities				
Acquisition of fixed assets	(16,235)	(9,339)	(16,305)	(16,235)
Proceeds from sale of fixed assets	197	635	800	93
Net cash used in investing activities	(16,038)	(8,704)	(15,505)	(16,142)
Cash flows - financing activities				

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Short-term bank credit, net	-	(18)	(4,147)	-
Repayment of long-term loans	(15,265)	(21,116)	(7,266)	(15,265)
Repayment of long-term capital notes to shareholders	(27,128)	(43,790)	-	(27,128)
	-----	-----	-----	-----
Net cash used in financing activities	(42,393)	(64,924)	(11,413)	(42,393)
	-----	-----	-----	-----
Increase (decrease) in cash and cash equivalents	(20,874)	(17,411)	20,818	(10,418)
Cash and cash equivalents - beginning of year	31,678	49,089	28,271	20,034
	-----	-----	-----	-----
Cash and cash equivalents - end of year	10,804	31,678	49,089	9,616
	=====	=====	=====	=====

(1) See Note 2A.

(2) Adjusted for changes in the exchange rate of the U.S. dollar as of December 31, 2003.

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

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MONDI BUSINESS PAPER HADERA LTD.  
(FORMERLY, NEUSIEDLER HADERA PAPER LTD.)  
APPENDICES TO STATEMENTS OF CASH FLOWS  
(NIS in thousands)

	Consolidated			Year ended December 31, 2004
	Year ended December 31,			
	2004	2003	2002	2004
	Reported	Adjusted	Adjusted	Reported
	Amounts (1)	Amounts (2)	Amounts (2)	Amounts (1)
	-----	-----	-----	-----
A. Adjustments to reconcile net income to net cash provided by operating activities				
Income and expenses items not involving cash flows:				
Equity in net losses (earnings) of subsidiaries	-	-	-	(71)
Depreciation and amortization	9,118	8,626	8,077	7,885
Deferred taxes, net	823	10,438	11,483	359
Increase (decrease) in liability for severance pay, net	(58)	14	5	(58)

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Capital loss (gain)				
from sale of fixed assets	(100)	215	84	(47)
Effect of exchange rate and linkage differences of long-term bank loans and long-term loan to subsidiary	(195)	1,460	(134)	(195)
Effect of exchange rate differences of long-term capital notes to shareholders	571	-	-	571
Changes in assets and liabilities:				
Decrease (increase)				
in trade receivables	(10,067)	7,247	(696)	-
Decrease (increase)				
in other receivables	(932)	752	9,025	574
Decrease (increase)				
in inventories	(1,160)	(9,533)	13,010	2,349
Increase (decrease) in trade payables	(220)	27,447	6,043	9,721
Increase (decrease) in American Israeli Paper Mills Group, net	16,247	(*) (1,612)	(*) (19,014)	(39,448)
Increase in Subsidiaries	-	-	-	48,966
Increase (decrease) in other Payables and accrued expenses	6,268	(*) (7,356)	(*) 3,776	249
	-----	-----	-----	-----
	20,295	37,698	31,659	30,855
	=====	=====	=====	=====
 B. Non-cash activities Acquisition of fixed assets on credit	 784	 -	 -	 784
	=====	=====	=====	=====

(\*) Reclassified.

(1) See Note 2A.

(2) Adjusted for changes in the exchange rate of the U.S. dollar as of December 31, 2003.

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

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MONDI BUSINESS PAPER HADERA LTD.  
(FORMERLY, NEUSIEDLER HADERA PAPER LTD.)  
NOTES TO FINANCIAL STATEMENTS

NOTE 1 - DESCRIPTION OF BUSINESS AND GENERAL

A. Description of Business

Mondi Business Paper Hadera Ltd. ("the Company") was incorporated and commenced operations on January 1, 2000. The Company and its Subsidiaries are engaged in the production and marketing of paper, mainly in Israel.

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Within the framework of a comprehensive decision of Neusiedler AG ("NAG" or the "Parent Company"), wholly-owned by the Mondi Group, the Company and one of its Subsidiaries changed their names in November 2004 to Mondi Business Paper Hadera Ltd. and Mondi Business Paper Hadera Marketing Ltd. in replacement of Neusiedler Hadera Paper Ltd. and Neusiedler Hadera Paper Marketing (1999) Ltd., respectively.

In the framework of a change in the organizational structure of the Group, effective January 1, 2003, all marketing and selling activities of the Group, which until such date were performed by four Subsidiaries, were centralized to one Subsidiary with three logistic sites.

The Company is presently owned by NAG (50.1%) and American-Israeli Paper Mills Ltd. ("AIPM") (49.9%).

### B. Definitions:

The Company	-	Mondi Business Paper Hadera Ltd.
The Group	-	the Company and its Subsidiaries, a list of which is provided in Note 7C.
Subsidiaries	-	companies in which the Company exercises over 50% ownership and control, directly or indirectly, and whose financial statements are fully consolidated with those of the Company.
Related Parties	-	as defined by Opinion No. 29 of the Institute of Certified Public Accountants in Israel.
Interested Parties	-	as defined in the Israeli Securities Regulation (Presentation of Financial Statements), 1993.
Controlling Shareholder	-	as defined in the Israeli Securities Regulation (Presentation of Transactions between a Corporation and its Controlling Shareholder in the Financial Statements), 1996.
NIS	-	New Israeli Shekel.
CPI	-	the Israeli consumer price index.
Dollar	-	the U.S. dollar.
Euro	-	the United European currency.
Adjusted Amount	-	see Note 2A(1) below.
Reported Amount	-	see Note 2A(1) below.

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MONDI BUSINESS PAPER HADERA LTD.  
(FORMERLY, NEUSIEDLER HADERA PAPER LTD.)  
NOTES TO FINANCIAL STATEMENTS

NOTE 1 - DESCRIPTION OF BUSINESS AND GENERAL (cont.)

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### C. Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements, and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

### NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES

The following are the principal accounting policies applied in the preparation of the financial statements in a manner consistent with previous years with the exception of the cessation of financial statement adjustment as described in paragraph A below.

#### A. Cessation of Financial Statement Adjustment and Change to Reporting in Reported Amounts - Standard No. 12

##### (1) Definitions

Adjusted Amount - historical nominal amount adjusted for changes in the exchange rate of the U.S. dollar as of December 31, 2003, in accordance with Opinion No. 36 of the Institute of Certified Public Accountants in Israel.

Reported Amount - Adjusted Amount plus amounts in nominal terms added subsequent to December 31, 2003, and less amounts subtracted after that date.

##### (2) General

In January 2004, Israeli Accounting Standard No. 12 "Cessation of Financial Statements Adjustment" came into effect. Following the initial implementation of Standard No. 12, commencing January 1, 2004, the Group ceased the presentation of its financial statements based on nominal historical cost adjusted for the changes in the exchange rate of the U.S. dollar in relation to the NIS. Effective with the interim financial statements as of March 31, 2004 and for the reporting periods thereafter, including the year ended December 31, 2004, the Group's financial statements are prepared and presented in Reported Amounts.

Comparative figures included in these financial statements relating to December 31, 2003 and for each of the two years then ended, are presented in Adjusted Amounts.

The amounts at which non-monetary items are presented in these financial statements do not necessarily represent their realization value or economic value, but solely their Reported Amount.

The Company's condensed financial statements in nominal values, on the basis of which the Company's financial statements in Reported amounts and Adjusted Amounts were prepared, are presented in Note 24.

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MONDI BUSINESS PAPER HADERA LTD.  
(FORMERLY, NEUSIEDLER HADERA PAPER LTD.)  
NOTES TO FINANCIAL STATEMENTS

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

A. Cessation of Financial Statement Adjustment and Change to Reporting in Reported Amounts - Standard No. 12 (cont.)

(3) Principles of Adjustment applicable for financial statements relating to reporting periods ended through December, 31 2003

a. Balance Sheet Items

Non-monetary items (items whose balances reflect historical value at acquisition or upon establishment) have been adjusted in accordance with the changes in the exchange rate of the U.S. dollar from the date of acquisition/establishment through December 31, 2003.

Monetary items (items whose balance sheet amount reflects their current value or realization value at the balance sheet date) are presented in the December 31, 2003 balance sheet at their nominal value as of that date.

Investments in Subsidiaries were presented based on the dollar adjusted financial statements of these companies.

b. Statement of Operations Items

Income and expenses reflecting transactions, other than financial income and expenses, were adjusted for changes in the exchange rate of the U.S. dollar from the date of the transaction through December 31, 2003.

Income and expenses deriving from non-monetary items (mainly depreciation, amortization, deferred taxes and changes in inventory) were presented in a manner corresponding to the adjustment of the related balance sheet items.

Financing income (expenses), net reflect income and expenses in real terms and include exchange rate differences derived from monetary items.

The Company's share in the results of Subsidiaries is determined based on the dollar adjusted financial statements of these companies.

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MONDI BUSINESS PAPER HADERA LTD.  
(FORMERLY, NEUSIEDLER HADERA PAPER LTD.)  
NOTES TO FINANCIAL STATEMENTS

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

A. Cessation of Financial Statement Adjustment and Change to Reporting in Reported Amounts - Standard No. 12 (cont.)

(4) Principles of Adjustment applicable for financial statements

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relating to reporting periods ended through December, 31 2004

### a. Balance Sheet Items

Non-monetary items (items whose balances reflect historical value at acquisition or upon establishment) are presented at their Adjusted Amounts plus additions and dispositions occurring during the reporting period. Additions made subsequent to December 31, 2003 and dispositions of items added subsequent to such date, are presented at their historical nominal value. Dispositions of items added on or prior to December 31, 2003 are presented at their Adjusted Amount.

Monetary items (items whose balance sheet amount reflects their current value or realization value at the balance sheet date) are presented at their nominal value as of the balance sheet date.

Investments in Subsidiaries are presented based on the financial statements of these companies prepared according to the guidance of Standard No. 12.

### b. Statement of Operations Items

Income and expenses reflecting transactions, and financial income and expenses, are presented at their nominal value.

Income and expenses deriving from non-monetary items (mainly depreciation, amortization and changes in inventory) were presented in a manner corresponding to the presentation of the related non-monetary balance sheet item, as illustrated above.

The Company's share in the results of Subsidiaries is determined based on the financial statements of these companies prepared according to the guidance of Standard No. 12.

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MONDI BUSINESS PAPER HADERA LTD.  
(FORMERLY, NEUSIEDLER HADERA PAPER LTD.)  
NOTES TO FINANCIAL STATEMENTS

## NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

### B. Principles of Consolidation

The consolidated financial statements include consolidation of the financial statements of all Subsidiaries. Material inter-company balances and transactions of and between Subsidiaries have been fully eliminated.

The data included in the consolidated financial statements is based on audited financial statements of the Subsidiaries included therein.

For amortization policy of an allocated goodwill associated with the acquisition of a Subsidiary, see H below.

### C. Cash and Cash Equivalents

Cash and cash equivalents include bank deposits, available for immediate withdrawal, as well as unrestricted short-term deposits with



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maturities of less than three months from the date of deposit.

### D. Allowance for Doubtful Accounts

The allowance for doubtful accounts is computed on the specific identification basis for accounts whose collectibility, on management's estimation, is uncertain.

### E. Inventories

Inventories are stated at the lower of cost or market value. Cost is determined for raw materials, auxiliary materials and finished products on the basis of weighted moving average cost per unit.

### F. Investments in Subsidiaries

Investments in Subsidiaries are presented using the equity method based on their audited financial statements. For amortization of an excess cost of an investment in a Subsidiary over its net book value at the acquisition date, see H below.

### G. Fixed Assets

Fixed assets are presented at cost less accumulated depreciation and amortization. Depreciation is calculated using the straight-line method at rates considered adequate to depreciate the assets over their estimated useful lives. Amortization of leasehold improvements is computed over the shorter of the term of the lease, including any option period, where the Company intends to exercise such option, or their useful life.

The annual depreciation and amortization rates are: %

Leasehold improvements	10
Machinery and equipment	5-20 (mainly 5%)
Motor vehicles	15-20
Office furniture and equipment	7-33

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MONDI BUSINESS PAPER HADERA LTD.  
(FORMERLY, NEUSIEDLER HADERA PAPER LTD.)  
NOTES TO FINANCIAL STATEMENTS

#### NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

### G. Fixed Assets (cont.)

#### Impairment of Long-Lived Assets

Management reviews long-lived assets on a periodic basis, as well as when such a review is required based upon relevant circumstances, to determine whether events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. According to the Israeli Accounting Standards Board's Standard No. 15, "Impairment of Assets", an asset's recoverable value is the higher of the asset's net selling price and the asset's value in use, the latter being equal to the asset's discounted expected cash flows. If applicable, an

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impairment loss is recorded at the amount in which the carrying amount of the asset exceeds its recoverable value.

### H. Other Assets - Goodwill

The unallocated excess cost of an investment in a Subsidiary over its net book value at the acquisition date reflects goodwill. The goodwill is amortized over the expected estimated economic life of the goodwill (10 years) by the straight-line method. Impairment examinations and recognition are performed and determined based on the accounting policy outlined in G above.

In March 2004, the Israeli Accounting Standards Board issued Standard No. 20 "The amortization Period of Goodwill". Standard No. 20 calls for the amortization of goodwill over its useful life, based on a systematic method that should reflect the estimated expected period in which the goodwill is to contribute economic benefits. The amortization period shall not exceed 20 years from the date on which the goodwill was initially recognized. Standard No. 20 is in effect for reporting periods commencing January 1, 2004, and its provisions are to be applied on a prospective basis. The implementation of Standard No. 20 did not, and is not expected to, affect the Group's financial position and results of operations.

### I. Supplier Discounts

Ongoing discounts granted by suppliers, as well as year end discounts, in respect of which no commitments to meet given targets are required by the Group, are included in the financial statements upon the execution of purchases that grant the Group said discounts. Supplier discounts contingent upon the Group's fulfillment of certain targets, such as meeting a minimal annual volume (in quantities or amount), or an increase in purchases over previous periods, are included in the financial statements in proportion to Group's purchases from suppliers during the reported period, which advance the Group towards the stated targets, only if it is expected that those targets will be reached and the discounts can reasonably be estimated. The estimate of meeting the targets is based, inter-alia, on historical experience, Group's relationships established with the suppliers and the estimated volume of purchases during the remaining reported period.

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MONDI BUSINESS PAPER HADERA LTD.  
(FORMERLY, NEUSIEDLER HADERA PAPER LTD.)  
NOTES TO FINANCIAL STATEMENTS

#### NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

### J. Deferred Income Taxes

The Group records deferred taxes in respect of temporary differences between the carrying values of assets and liabilities in the financial statements and their values for tax purposes, including depreciation differences on leased property and fixed assets. The Group records deferred-tax assets in respect of temporary difference as well as in respect of carry-forward tax losses so long as it is probable that those assets will be realized in the foreseeable future. The deferred taxes are computed by the tax rates expected to be in effect at

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realization, as they are known at the balance sheet date.

The computation of deferred taxes has not taken into account taxes that would have been applicable in case of future realization of investments in Subsidiaries, since the Group does not contemplate such realization in the foreseeable future.

### K. Revenue Recognition

Revenues are recognized upon shipment, when title has been transferred and collectibility is reasonably assured. Revenues are presented net of discounts granted. The accrual for estimated discounts granted is computed according to the provisions stipulated in the agreements, and is recorded when revenues are recognized.

### L. Forward Transactions

The gain or loss of currency forward transactions designated to hedge long-term loans from banks against currency fluctuations, are included in operations as incurred.

### M. Earnings Per Share

Earnings per share are computed based on the weighted average number of paid up capital shares during the year.

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MONDI BUSINESS PAPER HADERA LTD.  
(FORMERLY, NEUSIEDLER HADERA PAPER LTD.)  
NOTES TO FINANCIAL STATEMENTS

#### NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

### N. Exchange Rates and Linkage Basis

- (1) Balances in foreign currency or linked thereto are included in the financial statements based on the representative exchange rates, as published by the Bank of Israel, that were prevailing at the balance sheet date.
- (2) Following are the changes in the representative exchange rate of the U.S. dollar and the Euro vis-a-vis the NIS and in the Israeli CPI:

As of:	Representative exchange rate of the Dollar (NIS per \$1)	CPI "in respect of" (in points)
	-----	-----
December 31, 2004	4.308	180.74
December 31, 2003	4.379	178.58
December 31, 2002	4.737	182.02
Increase (decrease) during the year ended:	%	%
	-	-

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December 31, 2004	(1.6)	1.2
December 31, 2003	(7.6)	(1.9)
December 31, 2002	7.3	6.5

(3) Exchange-rate differences are charged to operations as incurred.

O. Reclassification

Certain amounts in prior years' financial statements have been reclassified in order to conform to the 2004 presentation.

P. Recent Accounting Standards - Income Taxes

In July 2004, the Israeli Accounting Standards Board published Accounting Standard No. 19 "Income Taxes" (the "Standard"). The Standard established the guideline for recognizing, measuring, presenting and disclosing taxes on income taxes in the financial statements. The Standard is effective for financial statements relating to reporting periods commencing on, or after, January 1, 2005. The initial adoption of the Standard shall be accounted for by the cumulative effect of change in accounting method, for the beginning of the period in which the Standard is initially adopted. The Company estimates that the implementation of the new Standard is not expected to have an effect on the Group's financial position, results of operations and cash flows.

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MONDI BUSINESS PAPER HADERA LTD.  
(FORMERLY, NEUSIEDLER HADERA PAPER LTD.)  
NOTES TO FINANCIAL STATEMENTS

NOTE 3 - CASH AND CASH EQUIVALENTS

	Consolidated	
	December	
	2 0 0 4	2 0 0 3
	Reported Amounts	Adjusted Amounts
	NIS in thousands	
In NIS	10,215	7,186
In foreign currencies (primarily the U.S. dollar)	589	24,492
	10,804	31,678
	=====	=====

NOTE 4 - TRADE RECEIVABLES

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	Consolidated	
	December 31,	
	2 0 0 4	2 0 0 3
	Reported Amounts	Adjusted Amounts
	NIS in thousands	
Composition:		
Domestic		
Open accounts	107,693	96,469
Checks receivable	29,943	35,952
	-----	-----
	137,636	132,421
	-----	-----
Foreign		
Open accounts	749	-
Related parties	21,872	18,957
	-----	-----
	22,621	18,957
	-----	-----
Less - allowance for doubtful accounts	2,442	3,630
	-----	-----
	157,815	147,748
	=====	=====

NOTE 5 - OTHER RECEIVABLES

	Consolidated	
	December	
	2 0 0 4	2 0 0 3
	Reported Amounts	Adjusted Amounts
	NIS in thousands	
Composition:		
Deferred taxes (Note 21D)	3,952	8,600
Prepaid expenses	842	990
Advances to suppliers	1,133	736
Value added tax	-	-
Income tax advances, net	240	201
Others	1,413	769
	-----	-----
	7,580	11,296
	=====	=====

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(FORMERLY, NEUSIEDLER HADERA PAPER LTD.)  
 NOTES TO FINANCIAL STATEMENTS

NOTE 6 - INVENTORIES

	Consolidated	
	December	
	2 0 0 4	2 0 0 3
	-----	-----
	Reported	Adjusted
	Amounts	Amounts
	-----	-----
	NIS in thousands	
Raw and auxiliary materials	30,098	31,389
Finished products (1)	60,293	57,842
	-----	-----
	90,391	89,231
	=====	=====
(1) Includes products in transit	1,723	-
	=====	=====
The inventories are net of provision for obsolescence	1,302	1,347
	=====	=====

NOTE 7 - INVESTMENTS IN SUBSIDIARIES

A. Composition NIS in thousands  
 Cost of shares  
 Accumulated losses since acquisition, net

Long-term loan (\*)

(\*) The non-interest bearing loan, denominated in NIS and linked to

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the Israeli Consumer Price Index, was considered part of the Company's investments in the Subsidiary. The loan was repaid at the end of 2004.

B. Goodwill: NIS in thousands

Cost  
Less - accumulated amortization

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NOTES TO FINANCIAL STATEMENTS

NOTE 7 - INVESTMENTS IN SUBSIDIARIES (cont.)

C. Consolidated Subsidiaries

The consolidated financial statements as of December 31, 2004, include the financial statements of the following Subsidiaries:

Mondi Business Paper Hadera Marketing Ltd. (see Note 1A)  
Grafinir Paper Marketing Ltd.  
Yavnir (1999) Ltd.  
Miterani Paper Marketing 2000 (1998) Ltd.

NOTE 8 - FIXED ASSETS

Machinery

Off  
furni

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	Leasehold improvements	and equipment	Motor vehicles	a equi
	-----	-----	-----	---
Consolidated	NIS in thousands			
Cost:				
Balance - January 1, 2004 (Adjusted Amounts)	3,724	(*) 124,390	1,785	2
Changes during 2004:				
Additions	-	16,155	811	
Dispositions	-	(317)	(311)	
	-----	-----	-----	---
Balance - December 31, 2004 (Reported Amounts) (1)	3,724	140,228	2,285	2
	-----	-----	-----	---
Accumulated depreciation:				
Balance - January 1, 2004 (Adjusted Amounts)	1,427	21,703	1,215	1
Changes during 2004:				
Additions	389	7,329	367	
Dispositions	-	(277)	(254)	
	-----	-----	-----	---
Balance - December 31, 2004 (Reported Amounts)	1,816	28,755	1,328	1
	-----	-----	-----	---
Net book value:				
December 31, 2004 (Reported Amounts)	1,908	111,473	957	1
	=====	=====	=====	=
December 31, 2003 (Adjusted Amounts)	2,297	102,687	570	1
	=====	=====	=====	=

(\*) Reclassified.

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MONDI BUSINESS PAPER HADERA LTD.  
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NOTES TO FINANCIAL STATEMENTS

NOTE 8 - FIXED ASSETS (cont.)

	Leasehold improvements	Machinery and equipment	Motor vehicles	Office furniture and equipment
	-----	-----	-----	-----
Company	NIS in thousands			
Cost:				
Balance - January 1, 2004 (Adjusted Amounts)	2,651	(*) 123,066	71	1,829
Changes during 2004:				
Additions	-	16,155	811	53



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Dispositions	-	(317)	(7)	-
	-----	-----	-----	-----
Balance - December 31, 2004 (Reported Amounts) (1)	2,651	138,904	875	1,882
	-----	-----	-----	-----
Accumulated depreciation:				
Balance - January 1, 2004 (Adjusted Amounts)	1,040	21,033	38	590
Changes during 2004:				
Additions	265	7,172	121	327
Dispositions	-	(277)	(1)	-
	-----	-----	-----	-----
Balance - December 31, 2004 (Reported Amounts)	1,305	27,928	158	917
	-----	-----	-----	-----
Net book value:				
December 31, 2004 (Reported Amounts)	1,346	110,976	717	965
	=====	=====	=====	=====
December 31, 2003 (Adjusted Amounts)	1,611	102,033	33	1,239
	=====	=====	=====	=====

(\*) Reclassified.

(1) Total cost as of December 31, 2004 includes payments on account of fixed asset in the amount of NIS 5,326 thousand.

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MONDI BUSINESS PAPER HADERA LTD.  
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NOTES TO FINANCIAL STATEMENTS

NOTE 9 - TRADE PAYABLES

	Consolidated	
	December 31	
	2004	2003
	Reported Amounts	Adjusted Amounts
	-----	-----
	NIS in thousands	
In Israeli currency	22,484	19,981
In foreign currency or linked thereto	82,177	84,116
	-----	-----
	104,661	104,097
	=====	=====

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NOTE 10 - OTHER PAYABLES AND ACCRUED EXPENSES

	Consolidated	
	December	
	2 0 0 4	2 0 0 3
	Reported Amounts	Adjusted Amounts
	NIS in thousands	
Accrued payroll and related expenses	11,703	(*) 11,900
Value Added Tax	3,366	368
Advances from customers	862	258
NAG - Parent Company	2,252	552
Interest payable	2,900	2,882
Forward transaction	1,322	-
Other	727	(*) 904
	-----	-----
	23,132	(*) 16,864
	=====	=====

(\*) Reclassified.

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MONDI BUSINESS PAPER HADERA LTD.  
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NOTES TO FINANCIAL STATEMENTS

NOTE 11 - LONG-TERM BANK LOANS

	Interest rate
	-----
	% (*)
A.Composition	
In U.S. dollar (**)	3.06
In Israeli CPI	6.55
Less - current maturities	

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(\*) Annual average interest rate as of December 31, 2004.

(\*\*) As of December 31, 2004, NIS 25,484 thousand bear interest based on Libor plus + 0.5%-0.6%.

B. Maturities

Second year - 2006  
 Third year - 2007  
 Fourth year - 2008  
 Fifth year - 2009  
 Sixth year - 2010 and thereafter

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C. According to the loan agreements with the banks, the Company is to achieve, inter alia, financial ratio at the end of each audited fiscal year of total shareholders equity including capital notes to shareholders to total assets to be no less than 30%. In case the Company fails to fulfill these covenants, the banks are entitled to demand early repayment of the loans, in whole or in part. As of December 31, 2004, the Company was in full compliance with the covenants stipulated in the bank agreements and this financial ratio amounted to 30.15%.

D. As to a "negative pledge agreement" signed by the Company, see Note 14B.

E. In 2004 and 2003, the Company and its Subsidiaries entered into an agreement for a bank credit facility, pursuant to which the Company and its subsidiaries may, from time to time, borrow an aggregate principal amount of up to adjusted NIS 87,580 thousand. Under the terms of the agreement, the credit facility has no time limit. As of the balance sheet date, the Group has not utilized any of the credit facility.

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### NOTE 12 - CAPITAL NOTES TO SHAREHOLDERS

The capital notes to shareholders are linked to the dollar and bear no interest. According to the terms of the capital notes, the Company has the ultimate discretion upon the dates of repayment of the capital notes. As of December 31, 2004, the Company has not yet determined the future repayment dates.

During 2004, the Company repaid the shareholders an aggregate of NIS 27,128 thousand (\$ 6,000 thousand) in respect of capital notes.

### NOTE 13 - ACCRUED SEVERANCE PAY, NET

Israeli law and labor agreements determine the obligations of the Group to make severance payments to dismissed employees and to employees leaving employment under certain other circumstances. The liability for severance pay benefits, as determined by Israeli Law, is based upon length of service and the employee's most recent monthly salary. The liability of the Group for severance pay to its permanent employees is covered by current deposits to pension and severance funds. Accumulated amounts so funded are not under the control or administration of the Group, and accordingly, neither those amounts nor the corresponding accruals are reflected in the financial statements. The amounts presented in the balance sheet as of December 31, 2004 reflects the severance pay liability in respect of temporary employees.

### NOTE 14 - COMMITMENTS AND CONTINGENT LIABILITIES

#### A. Commitments

- (1) The Group is obligated to pay license fees to a shareholder - see Note 22B.
- (2) The Company and its Subsidiaries lease certain of their facilities under operating leases for varying periods with renewal options primarily from AIPM. Future minimum lease rentals as of December 31, 2004 are as follows:

	Consolidated	Company
	-----	-----
	Reported amounts	
	-----	
	NIS in thousands	
	-----	
2005	4,599	3,446
2006	4,599	3,446
2007	4,599	3,446
2008	4,453	3,446
	-----	-----
	18,250	13,784
	=====	=====

#### B. Liens

To secure long-term bank loans and short-term bank credit (the balance of which as of December, 31 2004 is NIS 51,373 thousand), the Company entered into a "negative pledge" agreement under which the Company is

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committed not to pledge any of its assets, excluding fixed pledges relating to assets financed by others, prior to the consent of the banks.

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NOTES TO FINANCIAL STATEMENTS

NOTE 14 - COMMITMENTS AND CONTINGENT LIABILITIES (cont.)

C. Guarantees

The Company from time to time and in the framework of its ongoing operations provides guarantees, the amount of which as of December, 31 2004 was NIS 4,058 thousand.

NOTE 15 - SHARE CAPITAL

A. As of December 31, 2004 and 2003, share capital is composed of ordinary shares of NIS 1.00 par value each. Authorized - 38,000 shares; issued and paid up - 1,000 shares.

B. Holders of ordinary shares are entitled to participate equally in the payment of cash dividends and bonus share (stock dividend) distributions and, in the event of the liquidation of the Company, in the distribution of assets after satisfaction of liabilities to creditors. See also Note 1A.

NOTE 16 - NET SALES

	Consolidated			
	Year ended December 31,			
	2 0 0 4	2 0 0 3	2 0 0 2	2 0 0 4
	Reported Amounts	Adjusted Amounts	Adjusted Amounts	Reported Amounts
NIS in thousands				
Industrial operations	471,190	(*) 453,807	(*) 422,885	482,698
Commercial operations	214,904	186,213	(*) 151,342	-
	-----	-----	-----	-----
	686,094	(*) 640,020	(*) 574,227	482,698
	=====	=====	=====	=====

(\*) Reclassified.

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MONDI BUSINESS PAPER HADERA LTD.  
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NOTES TO FINANCIAL STATEMENTS

NOTE 17 - COST OF SALES

	Consolidated			Year ended December 31, 2 0 0 4
	Year ended December 31,			
	2 0 0 4	2 0 0 3	2 0 0 2	
	Reported Amounts	Adjusted Amounts	Adjusted Amounts	
	NIS in thousands			NIS
Purchases (**)	188,013	177,176	122,125	-
Materials consumed	297,006	271,334	251,070	297,006
Salaries and related expenses	32,576	30,482	(*) 27,358	32,576
Subcontracting	5,066	(*) 4,388	(*) 2,951	5,06
Energy costs	45,991	43,166	36,539	45,991
Depreciation	7,896	7,243	6,464	7,897
Other manufacturing costs and expenses (including rent)	31,124	(*) 30,370	(*) 26,230	30,335
	607,672	564,159	472,737	418,871
Change in finished goods and goods in process	(1,934)	(7,269)	18,975	(2,367)
	605,738	556,890	(*) 491,712	416,504
	=====	=====	=====	=====

(\*) Reclassified.

(\*\*) The purchases of the Group are related principally to commercial operations.

NOTE 18 - SELLING EXPENSES

	Consolidated			Year ended December 31, 2 0 0 4
	Year ended December 31,			
	2 0 0 4	2 0 0 3	2 0 0 2	
	Reported Amounts	Adjusted Amounts	Adjusted Amounts	
	NIS in thousands			NIS
Salaries and related expenses	17,169	16,913	(*) 16,440	17,169
Packaging and shipping to customers	16,235	(*) 14,368	(*) 14,460	15,464
Maintenance and rent	7,973	(*) 7,641	(*) 7,195	313
Transportation expenses	1,256	1,178	1,427	1,137
Advertising	-	180	153	-
Commissions and license fees to a shareholder	2,912	1,865	176	-

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Depreciation	552	670	880	523
Other	38	(*) 77	(*) -	-
	-----	-----	-----	-----
	46,135	42,892	(*) 40,731	34,606
	=====	=====	=====	=====

(\*) Reclassified.

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MONDI BUSINESS PAPER HADERA LTD.  
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NOTES TO FINANCIAL STATEMENTS

NOTE 19 - GENERAL AND ADMINISTRATIVE EXPENSES

	Consolidated			Year ----- 2 0 0 4 ----- Reported Amounts -----
	Year ended December 31,			
	2 0 0 4	2 0 0 3	2 0 0 2	
	Reported Amounts	Adjusted Amounts	Adjusted Amounts	
				Year ----- 2 0 0 4 ----- Reported Amounts -----
	NIS in thousands			
Salaries and related expenses	3,811	3,821	3,310	3,811
Office maintenance	187	(*) 232	(*) 696	-
Professional and management fees	2,217	1,594	2,227	1,555
Depreciation	47	(*) 28	(*) 110	40
Amortization of goodwill	623	(*) 623	(*) 623	-
Bad and doubtful debts	(311)	679	1,475	-
Other	1,229	(*) 1,448	(*) 1,771	1,036
	-----	-----	-----	-----
	7,803	(*) 8,425	(*) 10,212	6,442
	=====	=====	=====	=====

(\*) Reclassified.

NOTE 20 - FINANCING EXPENSES, NET

	Consolidated			Year en ----- 2 0 0 4 ----- Reported Amounts -----
	Year ended December 31,			
	2 0 0 4	(*) 2 0 0 3	(*) 2 0 0 2	
	Reported Amounts	Adjusted Amounts	Adjusted Amounts	
				Year en ----- 2 0 0 4 ----- Reported Amounts -----
	NIS in thousands			

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Interest on long-term bank loans	2,573	3,254	4,208	2,573
	=====	=====	=====	=====
Erosion of monetary assets and liabilities, net	2,070	(783)	(1,210)	1,293
	=====	=====	=====	=====
Forward transaction	1,322	-	-	1,322
	=====	=====	=====	=====

(\*) Reclassified.

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MONDI BUSINESS PAPER HADERA LTD.  
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NOTES TO FINANCIAL STATEMENTS

NOTE 21 - INCOME TAXES

A. The Company and its Subsidiaries are taxed according to the provisions of The Income Tax Ordinance and the Income Tax Law (Inflationary Adjustments), 1985. The Company is an industrial company in conformity with the Law for the Encouragement of Industry (Taxes), 1969. The major benefits the Company is entitled to under this law is accelerated depreciation rates.

	Consolidated			Year end 2 0 0 4
	Year ended December 31,			
	2 0 0 4	2 0 0 3	2 0 0 2	
	Reported Amounts	Adjusted Amounts	Adjusted Amounts	Reported Amounts
B. Composition	NIS in thousands			NIS
Current taxes	81	80	51	-
Taxes in respect of prior years	(86)	-	-	-
Deferred taxes (E. below)	823	10,438	11,483	359
	===	=====	=====	===
	818	10,518	11,534	359
	===	=====	=====	===

C. Reconciliation of the Statutory Tax Rate to the Effective Tax Rate

	Consolidated			Year end 2 0 0 4
	Year ended December 31,			
	2 0 0 4	(*) 2 0 0 3	(*) 2 0 0 2	



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	Reported Amounts	Adjusted Amounts	Adjusted Amounts	Reported Amounts
	NIS in thousands			
Income before income taxes	18,080	29,037	27,611	17,550
Tax computed by statutory tax rate (35%-36% - see E. below)	6,328	10,453	9,940	6,143
Tax increments (savings) due to:				
Non-deductible expenses	211	226	239	-
Non-taxable income	(40)	-	(94)	(21)
Reduction in corporate tax rates - (E. below)	(4,397)	-	-	(4,479)
Differences arising from basis of measurement (**)	(1,198)	(161)	1,449	(1,284)
Prior years income taxes	(86)	-	-	-
	818	10,518	11,534	359

(\*) Reclassified.

(\*\*) For 2004 - Reported Amounts (NIS) for financial reporting purposes vis-a-vis the consumer price index for tax purposes; For 2003 and 2002 - U.S. dollar for financial reporting purposes vis-a-vis the Consumer Price Index for tax purposes.

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MONDI BUSINESS PAPER HADERA LTD.  
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NOTES TO FINANCIAL STATEMENTS

NOTE 21 - INCOME TAXES (cont.)

D. Deferred Taxes

	Consolidated			
	Year ended December 31,			Year
	2 0 0 4	2 0 0 3	2 0 0 2	2 0 0 4
	Reported Amounts	Adjusted Amounts	Adjusted Amounts	Reported Amounts
	NIS in thousands			
Balance as of beginning of year	(20,647)	(10,209)	1,274	(22,135)
Changes during the year	(5,220)	(10,438)	(11,483)	(4,838)
Adjustment due to				

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change in income tax rates	4,397	-	-	4,479
	-----	-----	-----	-----
Balance as of end of year	(21,470)	(20,647)	(10,209)	(22,494)
	=====	=====	=====	=====

	Consolidated		Compan
	December 31,		
	2 0 0 4	2 0 0 3	2 0 0 4
	Reported	Adjusted	Reported
	Amounts	Amounts	Amounts
	-----	-----	-----
	NIS in thousands		NIS in tho
Deferred taxes are presented in the balance sheets as follows:			
Long-term liabilities:			
Depreciable fixed assets	(25,448)	(29,299)	(25,448)
Accrued severance pay, net	26	52	26
	-----	-----	-----
	(25,422)	(29,247)	(25,422)
	-----	-----	-----
Other receivables and prepayments (Note 5):			
Inventories	-	544	-
Allowance for doubtful accounts	831	1,308	-
Vacation and recreation pay	1,564	1,518	1,564
Carry forward tax losses	1,557	5,230	1,364
	-----	-----	-----
	3,952	8,600	2,928
	-----	-----	-----
	(21,470)	(20,647)	(22,494)
	=====	=====	=====

For 2004 - Deferred taxes were computed at rates between 30%-34%, primarily - 30%.

For 2003 - Deferred taxes were computed at 36%.

E. Reduction of Corporate Tax Rates

In June 2004, the Israeli Knesset passed Amendment No. 140 to the Income Tax Ordinance, according to which the corporate income-tax rate would be gradually reduced from 36% to 30% by 2007 (2004-35%, 2005-34%, 2006-32%, 2007-30%).

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NOTES TO FINANCIAL STATEMENTS

NOTE 21 - INCOME TAXES (cont.)

F. Carryforward tax losses of the Group and the Company are NIS 4,362 thousand

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and NIS 4,010 thousand as of December 31, 2004, respectively.

- G. The Company and its Subsidiaries have tax assessments that are considered final through the 2000 tax year.

NOTE 22 - RELATED PARTIES AND INTERESTED PARTIES

A. Balances with Related Parties and Subsidiaries

	Consolidated	
	December	
	2 0 0 4	2 0 0 3
	Reported Amounts	Adjusted Amounts
	NIS in thousands	
Trade receivables - AIPM	-	-
Trade receivables - related parties	21,872	18,957
Long-term loan to Subsidiary	-	-
Trade payables - AIPM	65,033	(*) 48,786
Trade payables - related parties	9,009	(*) 9,536
Other payables and accrued expenses - AIPM	2,478	(*) 2,298
Other payables and accrued expenses - related parties	2,252	(*) 552
Capital notes to shareholders	17,233	43,790

(\*) Reclassified.

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NOTES TO FINANCIAL STATEMENTS

NOTE 22 - RELATED PARTIES AND INTERESTED PARTIES (cont.)

B. Transactions with Related Parties and Subsidiaries

Consolidated			Comp	
Year ended December 31,			Year ended D	
2 0 0 4	2 0 0 3	2 0 0 2	2 0 0 4	2 0 0

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	Reported Amounts	Adjusted Amounts	Adjusted Amounts	Reported Amounts	Adjusted Amounts
	NIS in thousands			NIS in thousands	
Sales to related parties	165,596	171,131	155,599	-	-
Sales to Subsidiaries	-	-	-	482,698	462,698
Cost of sales	106,546	(*) 88,613	(*) 75,716	78,400	(*) 73,400
Selling expenses, net (Participation in selling expenses, net)	9,875	(*) 6,428	(*) -	1,796	(*) (1,796)
General and administrative expenses	1,837	(*) 1,410	(*) 1,756	1,480	(*) 1,480
Financing expenses (income), net	1,939	13,759	(3,722)	2,268	2,268

(\*) Reclassified.

(\*\*) The transactions as above are in the ordinary course of business at market prices and customary credit terms.

C. (1) The Company leases its premises from AIPM and render services (including electricity, water, maintenance and professional services) under agreements, which are renewed every year.

(2) The Group is obligated to pay commissions and license fees to NAG.

NOTE 23 - DISCLOSURE AND PRESENTATION OF FINANCIAL INSTRUMENTS

A. Credit Risk

The revenues of the Group's are derive from a large number of customers mainly in Israel and in Europe. Management regularly monitors the balance of trade receivables and the financial statements include an allowance for doubtful accounts based on management's estimation. Taking the aforementioned into consideration, the exposure to credit risk from trade receivables is immaterial.

Cash and cash equivalent (including amounts in foreign currency) are deposited with major commercial banks in Israel.

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NOTES TO FINANCIAL STATEMENTS

NOTE 23 - DISCLOSURE AND PRESENTATION OF FINANCIAL INSTRUMENTS (cont.)

B. Fair Value of Financial Instruments

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The financial instruments of the Group consist primarily of non-derivative assets and liabilities. Non-derivative assets include cash and cash equivalents, receivables, other current assets and long-term loans given. Non-derivative liabilities include trade payables, other current liabilities, long-term loans from banks and capital notes to shareholders. Due to the nature of these financial instruments, their fair value, generally, is identical or close to the value at which they are presented in the financial statements, unless stated otherwise.

The fair value of the long-term loans approximates their carrying value, since they bear interest at rates close to the prevailing market rates.

The terms of the Capital Notes to shareholders do not include determined payment dates. Therefore, fair value based on present values cannot be established and accordingly is not disclosed in the financial statements.

The Group maintains enters from time to time, into off-balance sheet financial instruments for hedging against currency and interest-rate risks.

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MONDI BUSINESS PAPER HADERA LTD.  
(FORMERLY, NEUSIEDLER HADERA PAPER LTD.)  
NOTES TO FINANCIAL STATEMENTS

NOTE 24 - COMPANY'S FINANCIAL STATEMENTS IN NOMINAL VALUES

A. Balance Sheets

	Compl
	----- Decemb -----
	2 0 0 4 ----- NIS in t
Current Assets	
Cash and cash equivalents	9,616
American Israeli Paper Mills Group, net	178,289
Other receivables	5,772
Inventories	60,301
	-----
	253,978
	-----
Long-Term Investments	
Investments in Subsidiaries	648
	=====
Fixed Assets, net	111,066
	-----
	365,692
	=====
Current Liabilities	

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Current maturities of long-term bank loans	15,125
Trade payables	63,902
Subsidiaries	99,159
Other payables and accrued expenses	16,480
	-----
	194,666
	-----
Long term liabilities	
Long term-bank loans	36,248
Capital notes to shareholders	17,233
Accrued severance pay, net	87
	-----
	53,568
	-----
Shareholders' Equity	117,458
	-----
	365,692
	=====

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MONDI BUSINESS PAPER HADERA LTD.  
(FORMERLY, NEUSIEDLER HADERA PAPER LTD.)  
NOTES TO FINANCIAL STATEMENTS

NOTE 24 - COMPANY'S FINANCIAL STATEMENTS IN NOMINAL VALUES (cont.)

B. Statement of Operations

	Year ended December 31,		
	2 0 0 4	2 0 0 3	2 0 0 2
	-----		
	NIS in thousands		
	-----	-----	-----
Net sales	482,698	480,764	452,986
Cost of sales	417,831	406,930	(*) 380,830
	-----	-----	-----
Gross profit	64,867	73,834	72,156
Selling expenses	34,598	33,455	(*) 26,929
General and administrative expenses	6,444	(*) 9,080	(*) 4,629
	-----	-----	-----
Operating profit	23,825	31,299	40,598
Financing (expenses) income, net	(7,143)	3,152	(11,957)
Other income (expenses), net	48	(*) (93)	(*) (10)
	-----	-----	-----
Income before income taxes	16,730	34,358	28,631

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Income taxes	-	-	-
	-----	-----	-----
Income after income taxes	16,730	34,358	28,631
Equity in net earnings (losses) of Subsidiaries	272	(34)	(385)
	-----	-----	-----
Net income for the year	17,002	34,324	28,246

(\*) Reclassified.

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MONDI BUSINESS PAPER HADERA LTD.  
(FORMERLY, NEUSIEDLER HADERA PAPER LTD.)  
NOTES TO FINANCIAL STATEMENTS

NOTE 24 - COMPANY'S FINANCIAL STATEMENTS IN NOMINAL VALUES (cont.)

C. Statements of Changes in Shareholders' Equity

	Share Capital	Premium	Retained earnings
	-----	-----	-----
	NIS in thousands		
Balance - January 1, 2002	1	41,125	(3,240)
	-----	-----	-----
Changes during 2002:			
Net income for the year	-	-	28,246
	-----	-----	-----
Balance - December 31, 2002	1	41,125	25,006
	-----	-----	-----
Changes during 2003:			
Net income for the year	-	-	34,324
	-----	-----	-----
Balance - December 31, 2003	1	41,125	59,330
	-----	-----	-----
Changes during 2004:			
Net income for the year	-	-	17,002
	-----	-----	-----
Balance - December 31, 2004	1	41,125	76,332
	=====	=====	=====

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EXHIBIT 5

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HOGLA-KIMBERLY LTD.  
FINANCIAL STATEMENTS  
AS OF DECEMBER 31, 2004

HOGLA-KIMBERLY LTD.  
FINANCIAL STATEMENTS  
AS OF DECEMBER 31, 2004

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## REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders of  
Hogla-Kimberly Ltd.

We have audited the accompanying balance sheets of Hogla-Kimberly Ltd. ("the Company") as of December 31, 2004 and 2003, and the consolidated balance sheets as of those dates, and the related statements of operations, changes in shareholders' equity and cash flows - of the Company and on a consolidated basis - for each of the three years in the period ended December 31, 2004. These financial statements are the responsibility of the Company's Board of Directors and management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audit in accordance with standards of the Public Company Accounting Oversight Board (United States) and with generally accepted auditing standards in Israel, including those prescribed by the Israeli Auditors' Regulations (Mode of Performance), 1973. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles



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used and significant estimates made by the Board of Directors and management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position - of the Company and on a consolidated basis - as of December 31, 2004 and 2003, and the results of operations, changes in shareholders' equity and cash flows - of the Company and on a consolidated basis - for each of the three years in the period ended December 31, 2004, in accordance with generally accepted accounting principles in Israel. In addition, in our opinion, the financial statements referred to above are prepared in accordance with the Israeli Securities Regulations (Preparation of Annual Financial Statements), 1993.

As explained in Note 2A, the financial statements as of dates and for reporting period commencing January 1, 2004, are presented at reported amounts, in accordance with accounting standards of the Israeli Accounting Standards Board. The financial statements as of dates prior to January 1, 2004 and for reporting periods ended through December 31, 2003, have been prepared on the basis of historical cost adjusted for changes in the exchange rate of the U.S. dollar in relation to the NIS, in accordance with pronouncements of the Institute of Certified Public Accountants in Israel.

Brightman Almagor & Co.  
 Certified Public Accountants  
 A Member Firm of Deloitte Touche Tohmatsu

Tel Aviv, March 7, 2005

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HOGLA-KIMBERLY LTD.  
 BALANCE SHEETS  
 (NIS in thousands)

		Consolidated	
		December 31,	
	Note	2 0 0 4	2 0 0 3
	----	-----	-----
		Reported	Adjusted
		Amounts (1)	Amounts (3)
		-----	-----
Current Assets			
Cash and cash equivalents	3	117,364	37,340
Current maturities of long-term bank deposits	7	-	7,882
Trade receivables	4	214,389	229,979
Other receivables	5	35,725	14,222
Inventories	6	142,551	92,664
		510,029	382,087
Long-Term Investments			
Long-term bank deposits	7	68,928	70,064
Capital note of shareholder	8	32,770	32,770
Investments in Subsidiaries	9	-	-
		-----	-----

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		101,698	102,834
		-----	-----
Fixed Assets	10		
Cost		507,175	479,744
Less - accumulated depreciation		222,256	210,176
		-----	-----
		284,919	269,568
		-----	-----
Other Assets			
Goodwill	9B	25,878	29,073
Deferred taxes	22	15,108	-
		-----	-----
		40,986	29,073
		-----	-----
		937,632	783,562
		=====	=====
Current Liabilities			
Short-term bank credit		-	1,087
Current maturities of			
long-term bank loans	13	68,747	15,147
Trade payables	11	219,902	139,555
Other payables and accrued expenses	12	38,720	37,632
		-----	-----
		327,369	193,421
		-----	-----
Long-Term Liabilities			
Long-term bank loans	13	81,851	96,338
Deferred taxes	22	37,388	29,428
		-----	-----
		119,239	125,766
		-----	-----
Commitments and Contingent Liabilities	15		
Minority Interest		54,492	51,394
		-----	-----
Shareholders' Equity			
Share capital	16	29,038	28,788
Capital reserves		180,414	156,799
Translation adjustments relating to			
foreign held autonomous Subsidiary (2)		(3,377)	-
Retained earnings		230,457	227,394
		-----	-----
		436,532	412,981
		-----	-----
		937,632	783,562
		=====	=====

(1) See Note 2A(1).

(2) See Note 2B.

(3) Adjusted for changes in the exchange rate of the U.S dollar as of December 31, 2003.

-----	-----	-----	-----
T. Davis	Y. Yerushalmi	O. Argov	A. Brenner
Chairman of the	Vice-Chairman of the	Chief Financial	Chief Executive
Board of Directors	Board of Directors	Officer	Officer

Approval date of the financial statements: March 7, 2005.

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

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HOGLA-KIMBERLY LTD.  
STATEMENTS OF OPERATIONS  
(NIS in thousands)

	Note	Consolidated			
		Year ended December 31,			
		2 0 0 4	2 0 0 3	2 0 0 2	2 0 0 1
		Reported Amounts (1)	Adjusted Amounts (2)	Adjusted Amounts (2)	Reported Amounts (1)
Net sales	17	995,569	868,671	766,549	479,000
Cost of sales	18	719,982	621,014	554,763	393,000
Gross profit		275,587	247,657	211,786	85,000
Selling expenses	19	193,701	130,670	123,955	150,000
General and administrative expenses	20	41,029	39,046	29,941	40,000
Operating profit		40,857	77,941	57,890	65,000
Financing income (expenses), net	21	(1,490)	5,517	(13,425)	(4,000)
Other income, net		903	496	78	0
Income before income taxes		40,270	83,954	44,543	60,000
Income taxes	22	10,244	20,566	19,232	17,000
Income after income taxes		30,026	63,388	25,311	43,000
Equity in net earnings (losses) of Subsidiaries		-	-	-	(16,000)
Minority interest in earnings of Subsidiary		(3,098)	(7,135)	(2,599)	0
Net income for the year		26,928	56,253	22,712	26,000
Earnings per share (in NIS) (*)		3.16	6.61	2.67	0.00
Number of shares used in computation (*)		8,513,473	8,513,473	8,513,473	8,513,473

(1) See Note 2A(1).

(2) Adjusted for changes in the exchange rate of the U.S dollar as of December

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31, 2003.

(\*) Retroactively adjusted for the effect of bonus share distribution.

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

HOGLA-KIMBERLY LTD.  
STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY  
(NIS in thousands)

	Share capital -----	Capital reserves -----	Translation adjustments relating to foreign held autonomous Subsidiary -----	Retained earnings -----
Balance - January 1, 2002 (Adjusted Amounts (3))	28,788	156,799	-	181,272
Changes during 2002:				
Dividend declared after balance-sheet date				(32,843)
Net income for the year				22,712
Balance - December 31, 2002 (Adjusted Amounts (3))	28,788	156,799	-	171,141
Changes during 2003:				
Dividend paid				
Net income for the year				56,253
Balance - December 31, 2003 (Adjusted Amounts (3))	28,788	156,799	-	227,394
Changes during 2004:				
Distribution of bonus shares	250	23,615		(23,865)
Translation adjustments relating to foreign held autonomous Subsidiary (2)			(3,377)	
Net income for the year				26,928
Balance - December 31, 2004 (Reported Amounts (1))	29,038	180,414	(3,377)	230,457

(1) See Note 2A(1).

(2) See Note 2B.

(3) Adjusted for changes in the exchange rate of the U.S dollar as of December 31, 2003.

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

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HOGLA-KIMBERLY LTD.  
STATEMENTS OF CASH FLOWS  
(NIS in thousands)

	Consolidated			
	Year ended December 31,			
	2 0 0 4	2 0 0 3	2 0 0 2	2 0 0 1
	Reported Amounts (1)	Adjusted Amounts (3)	Adjusted Amounts (3)	Reported Amounts (3)
Cash flows - operating activities				
Net income	26,928	56,253	22,712	26,928
Adjustments to reconcile net income to net cash provided by operating activities (Appendix A)	30,683	4,190	14,324	60,443
Net cash provided by operating activities	57,611	60,443	37,036	87,371
Cash flows - investing activities				
Withdrawal of short-term bank deposit	-	-	57,069	-
Withdrawal of long-term bank deposits	8,138	9,195	8,759	8,138
Acquisition of fixed assets	(25,191)	(26,953)	(76,523)	(17,000)
Proceeds from sale of fixed assets	1,827	1,092	456	1,827
Net cash used in investing activities	(15,226)	(16,666)	(10,239)	(8,035)
Cash flows - financing activities				
Dividend paid	-	(32,843)	(43,790)	-
Long-term loans received	57,672	28,949	11,386	57,672
Repayment of long-term loans	(15,162)	(24,960)	-	(15,162)
Short-term bank credit	(1,087)	1,087	-	(1,087)
Net cash provided by (used in) financing activities	41,423	(27,767)	(32,404)	(1,566)
Translation adjustments of cash and cash equivalents of foreign held autonomous Subsidiary (2)	(3,784)	-	-	(3,784)
Increase (decrease) in cash and cash equivalents	80,024	16,010	(5,607)	78,423
Cash and cash equivalents -				

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beginning of year	37,340	21,330	26,937	31
	-----	-----	-----	-----
Cash and cash equivalents - end of year	117,364	37,340	21,330	109
	=====	=====	=====	=====

- (1) See Note 2A(1).  
(2) See Note 2B.  
(3) Adjusted for changes in the exchange rate of the U.S dollar as of December 31, 2003.

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

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HOGLA-KIMBERLY LTD.  
APPENDICES TO STATEMENTS OF CASH FLOWS  
(NIS in thousands)

	Consolidated			
	Year ended December 31,			Year
	2 0 0 4	2 0 0 3	2 0 0 2	2 0 0 4
Reported Amounts (1)	Adjusted Amounts (2)	Adjusted Amounts (2)	Reported Amounts (1)	
	-----	-----	-----	-----
A. Adjustments to reconcile net income to net cash provided by operating activities				
Income and expenses items not involving cash flows:				
Minority interest in earnings of Subsidiary	3,098	7,135	2,599	-
Equity in net losses (earnings) of Subsidiaries	-	-	-	16,260
Depreciation and amortization	23,468	25,213	22,086	14,702
Deferred taxes, net	(5,011)	8,251	1,072	8,512
Loss (gain) from sale of fixed assets	(1,162)	(482)	81	(205)
Effect of exchange rate differences, net	(1,901)	(2,266)	2,202	(258)
Changes in assets and liabilities:				
Decrease (increase) in trade receivables	15,763	(47,933)	(14,411)	1,799
Decrease (increase) in other receivables	(20,938)	(2,115)	4,860	(6,211)

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Increase in inventories	(46,919)	(6,237)	(16,362)	(12,646)
Increase in trade payables	49,624	27,544	18,343	8,392
Net change in balances with related parties	13,591	(10,050)	7,731	28,985
Increase (decrease) in other payables and accrued expenses	1,070	5,130	(13,877)	1,604
	-----	-----	-----	-----
	30,683	4,190	14,324	60,934
	-----	-----	-----	-----

B. Non-cash activities

Acquisition of fixed assets on credit	18,470	8,661	13,707	11,619
---------------------------------------	--------	-------	--------	--------

- (1) See Note 2A(1).  
(2) Adjusted for changes in the exchange rate of the U.S dollar as of December 31, 2003.

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

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HOGLA-KIMBERLY LTD.  
NOTES TO FINANCIAL STATEMENTS

NOTE 1 - GENERAL

A. Description

Hogla Kimberly Ltd. ("the Company") and its Subsidiaries are engaged principally in the production and marketing of paper and hygienic products. The Company's results of operations are affected by transactions with shareholders and affiliated companies (see Note 23).

The Company is presently owned by Kimberly Clark Corp. ("KC" or the "Parent Company") (50.1%) and American-Israeli Paper Mills Ltd. ("AIPM") (49.9%).

B. Definitions:

The Company -	Hogla-Kimberly Ltd.
The Group -	the Company and its Subsidiaries, a list of which is provided in Note 9D.
Subsidiaries -	companies in which the Company exercises over 50% ownership and control, directly or indirectly, and whose financial statements are fully consolidated with those of the Company.
Related Parties -	as defined by Opinion No. 29 of the Institute of Certified Public Accountants in Israel.

Interested Parties - as defined by the Israeli Securities Regulations  
(Presentation of Financial Statements), 1993.

Controlling Shareholder as defined by the Israeli Securities Regulations  
(Presentation of Transactions between a Corporation  
and its Controlling Shareholder in the Financial  
Statements), 1996.

NIS - New Israeli Shekel.

CPI - the Israeli consumer price index.

Dollar - the U.S. dollar.

Adjusted Amount - see Note 2A(1) below.

Reported Amount - see Note 2A(1) below.

C. Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements, and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

D. The financial statements of the Company are prepared in accordance with the Israeli Securities Regulations (Preparation of Annual Financial Statements), 1993.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES

The following are the principal accounting policies applied in the preparation of the financial statements in a manner consistent with previous years with the exception of the cessation of financial statement adjustment as described in paragraph A below and Translation of Foreign Operations as described in paragraph B below.

A. Cessation of Financial Statements Adjustment and Change to Reporting in Reported Amounts - Standard No. 12

(1) Definitions

Adjusted Amount - historical nominal amount adjusted for changes in the exchange rate of the U.S. dollar as of December 31, 2003, in accordance with Opinion No. 36 of the Institute of Certified Public Accountants in Israel.

Reported Amount - Adjusted Amount plus amounts in nominal terms added subsequent to December 31, 2003, and less amounts subtracted after that date.



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### (2) General

In January 2004, Israeli Accounting Standard No. 12 "Cessation of Financial Statements Adjustment" came into effect. Following the initial implementation of Standard No. 12, commencing January 1, 2004, the Group ceased the presentation of its financial statements based on nominal historical cost adjusted for the changes in the exchange rate of the U.S. Dollar in relation to the NIS. Effective with the interim financial statements as of March 31, 2004 and for the reporting periods thereafter, including the year ended December 31, 2004, the Group's financial statements are prepared and presented in Reported Amounts.

Comparative figures included in these financial statements relating to December 31, 2003 and for each of the two years then ended, are presented in Adjusted Amounts.

The amounts at which non-monetary items are presented in these financial statements do not necessarily represent their realization value or economic value, but solely their Reported Amount.

The Company's condensed financial information in nominal values, on the basis of which the Company's financial statements in Reported Amounts and Adjusted Amounts were prepared, are presented in Note 25.

### (3) Basis of presentation

#### a. Balance Sheet Items

Non-monetary items (items whose balances reflect historical value at acquisition or upon establishment) are presented at their Adjusted Amounts plus additions and dispositions occurring during the reporting period. Additions made subsequent to December 31, 2003 and dispositions of items added subsequent to such date, are presented at their historical nominal value. Dispositions of items added on or prior to December 31, 2003 are presented at their Adjusted Amount.

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## NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

### A. Cessation of Financial Statements Adjustment and Change to Reporting in Reported Amounts - Standard No. 12 (cont.)

#### (3) Basis of presentation (cont.)

##### a. Balance Sheet Items (cont.)

Monetary items (items whose balance sheet

amount reflects their current value or realization value at the balance sheet date) are presented at their nominal value as of the balance sheet date.

Investments in Subsidiaries and minority interest are presented based on the financial statements of these companies prepared according to the guidance of Standard No. 12.

b. Statement of Operations Items

Income and expenses reflecting transactions, and financial income and expenses, are presented at their nominal value.

Income and expenses deriving from non-monetary items (mainly depreciation and amortization) were presented in a manner corresponding to the presentation of the related non-monetary balance sheet item, as illustrated above.

The Company's share and minority interest in the results of Subsidiaries are determined based on the financial statements of these companies prepared according to the guidance of Standard No. 12.

(4) Principles of Adjustment through December 31, 2003

a. Balance Sheet Items

Non-monetary items (items whose balances reflect historical value at acquisition or upon establishment) have been adjusted in accordance with the changes in the exchange rate of the U.S. dollar from the date of acquisition/establishment through December 31, 2003.

Investments in Subsidiaries and minority interest were determined based on the dollar adjusted financial statements of these companies.

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NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

Monetary items (items whose balance sheet amounts represent current or realization value at the balance sheet date) are presented in the December 31, 2003 balance sheet at their nominal value as of that date.

b. Statement of Operations Items

Income and expenses reflecting transactions,

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other than financial income and expenses, were adjusted for changes in the exchange rate of the U.S. dollar from the date of the transaction to the balance sheet date.

Income and expenses arising from non-monetary items (mainly depreciation, amortization, deferred taxes and changes in inventory) were adjusted in a manner corresponding to the adjustment of the related balance sheet items.

(4) Principles of Adjustment through December 31, 2003  
(cont.)

b. Statement of Operations Items (cont.)

Financing income (expenses), net reflect income and expenses in real terms and include exchange rate differences derived from monetary items.

The Company's share and the minority interest in the results of Subsidiaries were determined based on the dollar adjusted financial statements of these companies.

c. Adjustment and Translation of Foreign Subsidiaries Financial Statements

The financial statements of Subsidiaries operating abroad, which act as an integral operation of the Group, were prepared in U.S. dollars and translated into NIS based on the exchange rate of the U.S. dollar on the balance sheet date.

B. Translation of Foreign Operations' Financial Statements -  
Standard No. 13

- (a) In January 2004, Israeli Accounting Standard No. 13 "Effect of Changes in Foreign Exchange Rates" came into effect. This Standard addresses the translation of transactions denominated in foreign currency, as well as the translation of financial statements of a foreign entity, for inclusion in the financial statements of the reporting company. Standard No. 13 supersedes Clarifications No. 8 and 9 to Opinion No. 36 of the Institute of Certified Public Accountants in Israel, which were nullified on the date on which Accounting Standard No. 12 came into effect, as described in A above.

- (b) A Foreign Entity Classified as a Foreign Held Autonomous Subsidiary
- o Following the implementation of Standard No. 13, commencing January 2004 goodwill derived from an investment made in another entity is to be treated as one of that entity's assets. Accordingly, the goodwill associated with the Group's investment in Ovisan (a Subsidiary located in Turkey) is translated to NIS at the closing rate, rather than at the exchange rate at the date in which said investment was made, as was previously required under the applicable accounting literature in effect through December 31, 2003.
  - o Monetary and non-monetary assets and liabilities of the foreign entity are translated at the closing rate.
  - o Statement of operations items and cash flow items of the foreign entity are translated, in general, by the average exchange rate for the reporting period, rather than by the closing rate as was previously required under the applicable accounting literature prior to the date in which Standard No. 13 came into effect (January 1, 2004).
  - o All differences resulting from the translation of the foreign entity's financial statements by the method described above, are included in a separate component of shareholders' equity as "Translation adjustments relating to foreign held autonomous Subsidiary".

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NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

C. Principles of Consolidation

The consolidated financial statements include consolidation of the financial statements of all Subsidiaries. Material inter-company balances and transactions of and between Subsidiaries and the Company have been fully eliminated.

The data included in the consolidated financial statements is based on audited financial statements of the Subsidiaries

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included therein.

The excess cost of an investment in a Subsidiary in Turkey over the net book value upon acquisition of that Subsidiary is allocated to fixed assets and is amortized at the rate applicable to those assets, or upon their realization. The unallocated excess cost reflects goodwill, which is presented in the consolidated balance sheet as "other assets" and amortized by the straight-line method over 15 years due to the unique economic conditions relating to that Subsidiary and the expected economic benefit period from its acquisition. See also I below.

D. Cash and Cash Equivalents

Cash and cash equivalents include bank deposits, available for immediate withdrawal, as well as unrestricted short-term deposits with maturities of less than three months from the date of deposit.

E. Allowance for Doubtful Accounts

The allowance for doubtful accounts is generally computed as percentage from the relevant balances, on the basis of historical experience, with the addition of a specific provision in respect of accounts, which on management estimate are doubtful of collection.

F. Inventories

Inventories are presented at the lower of cost or market value, with cost determined as follows:

Finished products	-	Based on actual production cost.
Raw, auxiliary materials and other	-	Based on moving-average basis.

G. Investments in Subsidiaries

Investments in Subsidiaries are presented using the equity method based on their audited financial statements. In relation to excess cost of investment in Subsidiary in Turkey, see C above.

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### NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

H. Fixed Assets

Fixed assets are presented at cost less accumulated depreciation and amortization. Depreciation is calculated using the straight-line method at rates considered adequate to depreciate the assets over their estimated useful lives. Amortization of leasehold improvements is computed over the shorter of the term of the lease, including any option period, where the Company intends to exercise such option, or their useful life.

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The annual depreciation and amortization rates are: %

Buildings	2-4
Leasehold improvements	10-25
Machinery and equipment	5-20
Motor vehicles	15-20
Office furniture and equipment	10-33

### Impairment of Long-Lived Assets

Management reviews long-lived assets on a periodic basis, as well as when such a review is required based upon relevant circumstances, to determine whether events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. According to Standard No.15 of the Israeli Accounting Standards Board, "Impairment of Assets", an asset's recoverable value is the higher of the asset's net selling price and the asset's value in use, the latter being equal to the asset's discounted expected cash flows. If applicable, an impairment loss is recorded at the amount in which the carrying amount of the asset exceeds its recoverable value.

#### I. Other Assets - Goodwill

Goodwill derived from the acquisition of Subsidiary in Turkey is amortized based on the straight line method over 15 years (see also C above). Impairment examinations and recognition are performed and determined based on the accounting policy outlined in H above. In March 2004, the Israeli Accounting Standard Board issued Standard No. 20 "The Amortization Period of Goodwill". Standard No. 20 calls for the amortization of goodwill over its useful life, based on a systematic method that should reflect the estimated expected period in which the goodwill is to contribute economic benefits. The amortization period shall not exceed 20 years from the date on which the goodwill was initially recognized. Standard No. 20 is in effect for reporting periods commencing January 1, 2004, and its provisions are to be applied on a prospective basis. The implementation of Standard No. 20 did not, and is not expected to, affect the Group's financial position and results of operations.

#### J. Supplier Discounts

Ongoing discounts granted by suppliers, as well as year end discounts, in respect of which no commitments to meet given targets are required by the Group, are included in the financial statements upon the execution of purchases that grant the Group said discounts. Supplier discounts contingent upon the Group's fulfillment of certain targets, such as meeting a minimal annual volume (in quantities or amount), or an increase in purchases over previous periods, are included in the financial statements in proportion to the Group's purchases from suppliers during the reported period, which advance the Group towards the stated targets, only if it is expected that those targets will be reached and the discounts can reasonably be estimated. The estimate of meeting the targets is based, inter-alia, on historical experience, Group's relationships established with the suppliers and the estimated volume of purchases during the remaining reported period.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

K. Deferred Income Taxes

The Group records deferred taxes in respect of temporary differences between the carrying values of assets and liabilities in the financial statements and their values for tax purposes, including depreciation differences on leased property and fixed assets. The Group records deferred-tax assets in respect of temporary differences as well as in respect of carry-forward tax losses so long as it is probable that those assets will be realized in the foreseeable future. The deferred taxes are computed by the tax rates expected to be in effect at realization, as they are known at the approval date of the financial statements.

The computation of deferred taxes has not taken into account taxes that would have been applicable in case of future realization of investments in Subsidiaries, since the Group does not contemplate such realization in the foreseeable future. Moreover, the computation also excludes deferred taxes in respect of dividend distributions within the Group for cases in which such dividend distributions are expected to be tax-exempt.

L. Dividends

Dividends proposed or declared subsequent to the balance-sheet date, but prior to the financial statements approval date, are presented as a separate component of shareholders' equity.

M. Revenue Recognition

Revenues are recognized upon shipment, when title has been transferred and collectibility is reasonably assured.

Revenues are presented net of sales incentives, primarily: bonuses granted to chains as a percentage of their purchases (target bonus); volume discounts; and coupons distributed to customers entitling price discounts.

An accrual for estimated returns and sales incentives, computed primarily on the basis of historical experience, is recorded at the time revenues are recognized and deducted from revenues.

N. Earnings Per Share

Earnings per share are computed based on the number of paid up capital shares during the year.

O. Exchange Rates and Linkage Basis

- (1) Balances in foreign currency or linked thereto are included in the financial statements based on the representative exchange rates, as published by the Bank of Israel, that were prevailing at the balance

sheet date.

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NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

O. Exchange Rates and Linkage Basis (cont.)

(2) Following are the changes in the representative exchange rate of the U.S. dollar vis-a-vis the NIS and the Turkish Lira, and in the CPI:

As of:	Representative exchange rate of the Dollar (NIS per \$1)	Turkish Lira rate with dollar (TL'000)
	-----	-----
December 31, 2004	4.308	1,
December 31, 2003	4.379	1,
December 31, 2002	4.737	1,
Increase (decrease) during the year ended:	%	%
	-----	-----
December 31, 2004	(1.6)	(2.
December 31, 2003	(7.6)	(15
December 31, 2002	7.3	13

(3) Exchange-rate differences are charged to operations as incurred.

P. Reclassification

Certain amounts in prior years' financial statements have been reclassified in order to conform to the 2004 presentation.

Q. Recent Accounting Standards - Income Taxes

In July 2004, the Israeli Accounting Standard Board published Accounting Standard No. 19 "Income Taxes" (the "Standard"). The Standard established the guidelines for recognizing, measuring, presenting and disclosing income taxes in the financial statements. The Standard is effective for financial statements relating to reporting periods commencing on, or after, January 1, 2005. The initial adoption of the Standard shall be accounted for by the cumulative effect of a change in accounting method, for the beginning of the period in which the Standard is initially adopted. The implementation of Standard No. 19 is not expected to affect the Group's financial position and results of operations.

NOTE 3 - CASH AND CASH EQUIVALENTS

Consolidated

Compan



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	December 31,		
	2 0 0 4	2 0 0 3	2 0 0 4
	Reported Amounts	Adjusted Amounts	Reported Amounts
	NIS in thousands		NIS in thousands
In NIS	875	527	589
In foreign currencies (primarily the U.S. dollar)	116,489	36,813	109,128
	<u>117,364</u>	<u>37,340</u>	<u>109,717</u>
	=====	=====	=====

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NOTE 4 - TRADE RECEIVABLES

	Consolidated	
	December 31	
	2 0 0 4	2 0 0 3
	Reported Amounts	Adjusted Amounts
	NIS in thousands	
Domestic - Open accounts	159,693	154,617
Checks receivable	33,013	34,421
Related parties	598	348
	<u>193,304</u>	<u>189,386</u>
Foreign - Open accounts	25,971	47,697
Related parties	775	206
	<u>220,050</u>	<u>237,289</u>
Less - allowance for doubtful accounts	5,661	7,310
	<u>214,389</u>	<u>229,979</u>
	=====	=====

The Company's products are marketed principally by its Subsidiaries.

NOTE 5 - OTHER RECEIVABLES

	Consolidated	
	December	
	2 0 0 4	2 0 0 3
	Reported	Adjusted

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	Amount -----	Amounts -----
	NIS in thousands	
Deferred taxes (Note 22D)	4,611	5,518
Prepaid expenses	2,175	2,908
Advances to suppliers	615	3,074
Value added taxes	15,970	236
Income tax advances, net	10,973	1,467
Loans to employees	600	477
Other	781	542
	-----	-----
	35,725	14,222
	=====	=====

(\* ) Reclassified.

NOTE 6 - INVENTORIES

	Consolidated -----	
	December	
	2 0 0 4 -----	2 0 0 3 -----
	Reported Amount	Adjusted Amounts
	-----	
	NIS in thousands	
Raw and auxiliary materials	67,765	48,482
Finished goods	56,872	29,087
Spare parts and other	17,914	15,095
	-----	-----
	142,551	92,664
	=====	=====

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NOTE 7 - LONG-TERM BANK DEPOSITS

	Interest rate -----	Consolidated -----	
	% (*)	December	
		2 0 0 4 -----	2 0 0 3 -----
		Reported Amounts	Adjusted Amounts
		-----	
		NIS in thousands	
A. Composition			
Linked to the U.S. dollar	1.75	68,928	77,946
Less - current			

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maturities	-	7,882
	-----	-----
	68,928	70,064

(\*) Annual interest rate as of December 31, 2004.

B. The deposit is held as collateral for long-term loan received by Subsidiary (see Note 15C).

C. The deposit is subject to re-deposit every two years.

NOTE 8 - CAPITAL NOTE OF SHAREHOLDER

The capital note of AIPM, denominated in NIS, is not linked and does not bear interest. Repayment date will be mutually agreed upon. The erosion or increase in value of the capital note was charged to capital reserves until March 31, 2000 (the date on which AIPM ceased to be the controlling shareholder).

NOTE 9 - INVESTMENTS IN SUBSIDIARIES

A. Composition

Cost of shares  
 Equity in post-acquisition earnings, net  
 Translation adjustments relating to  
 foreign held autonomous Subsidiary  
 Capital notes (\*)

(\*) The non-interest bearing capital notes, denominated in U.S. dollar, are considered part of the Company's investments in the Subsidiaries. Repayment dates have not yet been determined.

NOTE 9 - INVESTMENTS IN SUBSIDIARIES (cont.)

B. Goodwill (see Note 2C above) NIS in thousands  
Cost  
Less - accumulated amortization

C. Investment in Ovisan

As of December 31, 2004, the Group's investment in the Turkish Subsidiary amounted to NIS 28,001 thousand (including goodwill in the net amount of NIS 25,878 thousand).

D. Consolidated Subsidiaries

The consolidated financial statements as of December 31, 2004, include the financial statements of the following Subsidiaries:

Rakefet Marketing and Trade Services Ltd. ("Rakefet")

Subsidiaries of Rakefet:

Hogla-Kimberly Marketing Ltd.

("Marketing")

Shikma Ltd. ("Shikma")

Mollet Marketing Ltd. ("Mollet")

H-K Overseas (Holland) B.V.

Subsidiaries of H-K Overseas (Holland) B.V.:

Ovisan Sihhi Bez Sanai ve Ticaret Anonim

Sirketi ("Ovisan")

Hogla-Kimberly Holding Anonim Sirketi

(\*) The remaining ownership and control of Rakefet are held by AIPM group (10.1%) and by KC (10.2%).

(\*\*) The remaining ownership and control of Marketing and Shikma are held by the Company.

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NOTE 10 - FIXED ASSETS

CONSOLIDATED	Buildings (1)	Leasehold improvements	Machinery and equipment	Motor vehicles
	-----	-----	-----	-----
Cost:	NIS in thousands			
Balance - January 1, 2004 (Adjusted Amounts)	54,869	9,268	384,618	19,048
Changes during 2004:				
Additions	1,184	111	33,679	334
Dispositions	-	-	(4,477)	(5,111)
Foreign currency translation adjustments	305	-	829	71
	-----	-----	-----	-----
Balance - December 31, 2004 (Reported Amounts)	56,358	9,379	414,649	14,342
	-----	-----	-----	-----
Accumulated depreciation:				
Balance - January 1, 2004 (Adjusted Amounts)	15,385	5,097	166,491	14,983
Changes during 2004:				
Additions	614	841	15,911	1,968
Dispositions	-	-	(3,946)	(4,985)
Foreign currency translation adjustments	112	-	519	63
	-----	-----	-----	-----
Balance - December 31, 2004 (Reported Amounts)	16,111	5,938	178,975	12,029
	-----	-----	-----	-----
Net book value:				
December 31, 2004 (Reported Amounts)	40,247	3,441	235,674	2,313
	=====	=====	=====	=====
December 31, 2003 (Adjusted Amounts)	39,484	4,171	218,127	4,065
	=====	=====	=====	=====
COMPANY				
Cost:				
Balance - January 1, 2004 (Adjusted Amounts)	25,209	6,112	343,089	3,159
Changes during 2004:				
Additions	116	111	29,816	334
Dispositions	-	-	(4,125)	(878)
	-----	-----	-----	-----
Balance - December 31, 2004 (Reported Amounts)	25,325	6,223	368,780	2,615
	-----	-----	-----	-----
Accumulated depreciation:				
Balance - January 1, 2004 (Adjusted Amounts)	11,812	3,733	142,932	3,076
Changes during 2004:				
Additions	-	589	13,876	18
Dispositions	-	-	(3,681)	(878)

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	-----	-----	-----	-----
Balance - December 31, 2004 (Reported Amounts)	11,812	4,322	153,127	2,216
Net book value: December 31, 2004 (Reported Amounts)	13,513	1,901	215,653	399
December 31, 2003 (Adjusted Amounts)	13,397	2,379	200,157	83

- (1) Buildings include industrial buildings on lands leased by the Company from AIPM (until 2005).  
(2) The majority of the Group's fixed assets are located in Israel.

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NOTE 11 - TRADE PAYABLES

	Consolidated		
			December 31
	2 0 0 4	2 0 0 3	
	Reported Amounts	Adjusted Amounts	R A
	NIS in thousands		
In Israeli currency			
Open accounts	112,932	78,509	
Related parties	23,124	13,682	
In foreign currency			
Open accounts	67,915	37,294	
Related parties	15,931	10,070	
	219,902	139,555	

NOTE 12 - OTHER PAYABLES AND ACCRUED EXPENSES

	Consolidated		
			December 31
	2 0 0 4	2 0 0 3	
	Reported Amounts	Adjusted Amounts	R A
	NIS in thousands		
Accrued income taxes, net of advances	10,464	8,663	
Accrued payroll and related expenses	22,195	20,531	1

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Value Added Tax	2,695	4,779
Advances from customers	726	1,085
Other	2,640	2,574
	-----	-----
	38,720	37,632
	=====	=====

NOTE 13 - LONG-TERM BANK LOANS

	Interest rate	
	-----	
	% (*)	
A. Composition		
In U.S. dollar	Libor +1.22-1.63	150
In Euro		68
Less - current maturities		-----
		81
		=====
(*) Annual interest rate as of December 31, 2004.		
B. Maturities (NIS in thousands)		
2005 - current maturities		68
2006		12
Thereafter - see C below		68
		-----
		150
		=====
C. Subject to renewal every two years - see Note 7C.		
D. Liens - see Note 15C.		

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NOTE 14 - SEVERANCE PAY

Obligations of the Group for severance pay to its employees are covered by current payments to pension and severance funds. Accumulated amounts in the pension and severance funds are not under the control or administration of the Group, and accordingly, neither those amounts nor the corresponding accruals are reflected in the financial statements.

NOTE 15 - COMMITMENTS AND CONTINGENT LIABILITIES

A. Commitments

- (1) The Group is obligated to pay royalties to a shareholder - see Note 23B.
- (2) The Company and its Subsidiaries lease certain of

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their facilities under operating leases for varying periods with renewal options. Future minimum lease rentals as of December 31, 2004 are as follows:

	Consolidated -----	Company -----
	NIS in thousands	
2005	13,966	5,763
2006	7,178	-
2007	7,178	-
2008	7,178	-
2009 and thereafter	25,122	-
	60,622	5,763

B. Guarantees

- (1) The Company is contingently liable in respect of a guarantee securing bank loans provided to a Subsidiary, the balance of which as of December 31, 2004 amounted to NIS 81,670 thousand.
- (2) As part of their normal course of business, the Subsidiaries provided third parties with bank guarantees for contract performance, the balance of which as of December 31, 2004 amounted to NIS 295 thousand.

C. Liens

As a collateral for long-term loans given to Subsidiary, the Group recorded a lien on its bank deposits, in the amount of NIS 68,928 thousand as of December 31, 2004.

D. Legal proceedings

- (1) The Company received on December 7, 2003 a claim and a petition that was filed in Tel-Aviv district court for the approval of a class action against the Company. According to the petition the Company has reduced the number of units of diapers in a package and thus misled the public according to the Israeli Consumer Protection Act. The plaintiffs estimate the scope of the class action to be NIS 18 million. The Company rejects the claim and intends to defend itself against the action. Based on the opinion of the Company's legal counsel for this matter, management is unable, at this stage, to estimate the possible outcome of the lawsuit. However, based on the legal counsels, management estimates that the Company has valid arguments to oppose the lawsuit and reasonable basis for denying it from being recognized as a class action. Therefore, no provision was recorded in the financial statements relating to this matter.



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D. Legal proceedings (cont.)

(2) In February 2004, a former customer filed a lawsuit against the Company. This lawsuit is a part of multi-suppliers lawsuit, filed by the customer and asking for one billion NIS from the Company and each other supplier for alleged damages. The customer asked for discharge from legal fee and the request was denied. Due to the preliminary stage of the proceedings, management is unable to estimate the possible outcome of the lawsuit. However, based on the Company's legal counsels, management estimates that the Company has valid arguments to oppose the lawsuit. Therefore, no provision was recorded in the financial statements relating to this matter.

NOTE 16 - SHARE CAPITAL

A. Composition of Share Capital in Nominal NIS

	As of December 31, 2004		As of D
	Authorized	Issued and fully paid up	Authorized
Ordinary Shares of Nis 1.00 par value	11,000,000	8,513,473	11,000,000

B. In connection with the Company's approved enterprise program, in September 2004, the Company's Board of Directors decided to issue to the Company's shareholders 250,000 bonus shares with a premium of NIS 94.46 for each share.

C. Holders of ordinary shares are entitled to participate equally in the payment of cash dividends and bonus share (stock dividend) distributions and, in the event of the liquidation of the Company, in the distribution of assets after satisfaction of liabilities to creditors. Each ordinary share is entitled to one vote on all matters to be voted on by shareholders.

NOTE 17 - NET SALES

	Conso	
	Year ended	
	2 0 0 4	2 0
	%	
A. Sales to major customers (as percentage from total net		

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sales)		
Customer A	9.9	8
Customer B	11.0	10

	NIS in t	
	Reported Amounts	Adju Amo
B. Sales from commercial operations	238,989	376
C. Foreign sales (principally Turkey)	108,102	106
	=====	=====

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NOTE 18 - COST OF SALES

	Consolidated			
	Year ended December 31,			Year
	2 0 0 4	2 0 0 3	2 0 0 2	2 0 0 4
	Reported Amounts	Adjusted Amounts	Adjusted Amounts	Reported Amounts
	NIS in thousands			N
Purchases (*)	558,155	446,008	425,365	239,402
Salaries and related expenses	85,167	67,516	55,999	62,870
Manufacturing expenses	87,201	79,810	55,834	84,717
Depreciation	17,244	18,221	14,207	14,674
	747,767	611,555	551,405	401,663
Change in finished goods inventory	(27,785)	9,459	3,358	(7,760)
	719,982	621,014	554,763	393,903
	=====	=====	=====	=====

(\*) The purchases of the Company are related to manufacturing operations. Consolidated purchases in excess of Company purchases relate principally to commercial operations.

NOTE 19 - SELLING EXPENSES

	Consolidated			
	Year ended December 31,			Year
	2 0 0 4	2 0 0 3	2 0 0 2	2 0 0 4

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	Reported Amounts -----	Adjusted Amounts -----	Adjusted Amounts -----	Reported Amounts -----
	NIS in thousands			
Salaries and related expenses	57,003	46,887	39,656	-
Maintenance and transportation expenses	42,283	26,596	24,332	7,206
Advertising and sales promotion	60,114	30,371	38,591	6,373
Commissions to distributors	5,130	4,571	2,007	-
Royalties to a shareholder	20,468	15,642	12,220	1,679
Depreciation	3,687	3,778	4,188	28
Other	5,016	2,825	2,961	-
	-----	-----	-----	-----
	193,701	130,670	123,955	15,286
	=====	=====	=====	=====

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NOTE 20 - GENERAL AND ADMINISTRATIVE EXPENSES

	Consolidated			
	Year ended December 31,			Year
	2 0 0 4	2 0 0 3	2 0 0 2	2 0 0 4
	Reported Amounts -----	Adjusted Amounts -----	Adjusted Amounts -----	Reported Amounts -----
	NIS in thousands			
Salaries and related expenses	15,837	18,283	13,481	2,387
Administrative and computer services	10,150	6,287	6,210	1,640
Services provided by Shareholder	1,188	1,161	1,161	238
Office maintenance	4,632	5,376	2,990	230
Depreciation	522	718	588	-
Goodwill amortization	2,832	2,768	2,768	-
Provision for doubtful accounts	2,144	1,562	215	-
Other	3,724	2,891	2,528	490
	-----	-----	-----	-----
	41,029	39,046	29,941	4,985
	=====	=====	=====	=====

NOTE 21 - FINANCING INCOME (EXPENSES), NET

	Consolidated			
	Year ended December 31,			Year e
	2 0 0 4	2 0 0 3	2 0 0 2	2 0 0 4
	-----	-----	-----	-----

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	Reported Amounts -----	Adjusted Amounts -----	Adjusted Amounts -----	Reported Amounts -----
	NIS in thousands			NIS
Interest on long-term bank loans	(2,673) =====	(2,111) =====	(2,794) =====	- =====
Exchange rate differences derived from capital note	- =====	2,476 =====	(2,202) =====	- =====
Interest from long-term and short-term bank deposits	1,464 =====	1,357 =====	1,804 =====	463 =====

The majority of the remaining balances of the consolidated financial income (expenses) for each of the periods presented are comprised of exchange rate differences.

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NOTE 22 - INCOME TAXES

	Consolidated			Consolidated	
	Year ended December 31,			Year ended	
	2 0 0 4 -----	2 0 0 3 -----	2 0 0 2 -----	2 0 0 4 -----	2 0 0 3 -----
	Reported Amounts -----	Adjusted Amounts -----	Adjusted Amounts -----	Reported Amounts -----	Adjusted Amounts -----
	NIS in thousands			NIS in thousands	
A. Composition					
Current taxes	18,045	10,878	18,904	9,952	
Taxes in respect of prior years	(1,003)	1,437	(744)	(837)	
Deferred taxes - D. below	(6,798) -----	8,251 -----	1,072 -----	8,512 -----	
	10,244 =====	20,566 =====	19,232 =====	17,627 =====	

B. The Company and its Israeli Subsidiaries are subject to the Income Tax Ordinance and the Income Tax Law (Inflationary Adjustments), 1985. Non-Israeli Subsidiaries are subject to income tax provisions of their home country. The Company is an industrial company in conformity with the Law for the Encouragement of Industry (Taxes), 1969. The principal benefit that the Company is entitled to under this law is accelerated depreciation rates and reduced tax rates.

During 2002, the Company's program for the establishment of a new facility for manufacturing paper was granted Approved Enterprise status in accordance with the Law for the Encouragement of Capital

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Investments, 1959, under "alternative benefits" track. The approval program is for total investments of approximately NIS 80 million. According to the terms of the program, income derived from the Approved Enterprise will be tax-exempt for a period of 10 years commencing in the year in which the program was substantially completed. Distribution of dividends from tax exempt profits of the Approved Enterprise will be subject to income tax at a rate equal to the income tax rate of the Approved Enterprise had the Company not elected the alternative benefits track. The Company completed the investments relating to the new facility and commenced its operations during 2003.

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NOTE 22 - INCOME TAXES (cont.)

C. Reconciliation of the statutory tax rate to the effective tax rate:

	Consolidated			Company	
	Year ended December 31,			Year ended Decem	
	2 0 0 4	2 0 0 3	2 0 0 2	2 0 0 4	2 0 0 3
Reported Amounts	Adjusted Amounts	Adjusted Amounts	Reported Amounts	Adjusted Amounts	
NIS in thousands			NIS in tho		
Income before income taxes	40,270	83,954	44,543	60,815	30,610
Tax computed by statutory tax rate (35%-36% - see E. below)	14,095	30,223	16,035	21,285	11,020
Tax increments (savings) due to:					
Reduced tax rate	(161)	(1,185)	(1,397)	(2,433)	(918)
Non-deductible expenses	1,454	1,874	1,840	6	434
Non-taxable income	(455)	(65)	(2,198)	(87)	-
Unrecorded deferred taxes in connection with tax loss carry forward	-	-	1,074	-	-
Utilization of prior years unrecorded deferred taxes in connection with tax loss carry forward	-	(3,471)	-	-	-
Unrecorded deferred taxes in connection with submitting consolidated tax returns	-	-	-	-	2,053
Reduction in corporate tax rates (E. below)	(1,594)	-	-	(1,573)	-

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Differences arising from

basis of measurement (*)	(2,821)	(7,629)	3,883	537	(1,753)
Income taxes for prior years	(1,003)	1,437	(744)	(837)	1,358
Other differences, net	729	(618)	739	729	(419)
	-----	-----	-----	-----	-----
	10,244	20,566	19,232	17,627	11,775
	=====	=====	=====	=====	=====

(\*) For 2004 - In Israel, Reported Amounts (NIS) for financial reporting purposes vis-a-vis the consumer price index for tax purposes; In Turkey - U.S. dollar for financial reporting purposes vis-a-vis the Turkish Lira for tax purposes.

For 2003 and 2002 - U.S. dollar for financial reporting purposes vis-a-vis the Consumer Price Index in Israel and the Turkish Lira for tax purposes.

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NOTE 22 - INCOME TAXES (cont.)

D. Deferred Taxes

	Consolidated			Company	
	Year ended December 31,			Year ended December	
	2 0 0 4	2 0 0 3	2 0 0 2	2 0 0 4	2 0 0 3
	-----	-----	-----	-----	-----
	Reported	Adjusted	Adjusted	Reported	Adjusted
	Amounts	Amounts	Amounts	Amounts	Amounts
	-----	-----	-----	-----	-----
	NIS in thousands			NIS in thousands	
Balance as of					
beginning of year	23,910	15,659	14,587	24,969	14,552
Changes during the year	(3,417)	8,251	1,072	10,085	10,417
Adjustment due to					
change in income					
tax					
rates	(1,594)	-	-	(1,573)	-
Foreign currency					
translation adjustments	(1,230)	-	-	-	-
	-----	-----	-----	-----	-----
Balance as of end					
of year	17,669	23,910	15,659	33,481	24,969

Consolidated			Company	
December 31,				
2 0 0 4	2 0 0 3	2 0 0 4	2 0 0 3	
-----	-----	-----	-----	-----

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	----- Reported Amounts ----- NIS in thousands	----- Adjusted Amounts ----- NIS in thousands	----- Reported Amounts ----- NIS in thousands	----- Adjusted Amounts ----- NIS in thousands
Deferred taxes are presented in the balance sheets as follows:				
Long-term liabilities (in respect of depreciable assets)	37,388	29,428	35,013	26,738
Other receivables (in respect of temporary differences) - Note 5	(4,611)	(5,518)	(1,532)	(1,769)
Other Assets	(15,108)	-	-	-
	----- 17,669 =====	----- 23,910 =====	----- 33,481 =====	----- 24,969 =====

For 2004 - Deferred taxes were computed at rates between 30%-34%, primarily - 30%. For 2003 - Deferred taxes were computed at rates between 32%-36%, primarily - 30%.

E. Reduction of Corporate Tax Rates

In June 2004, the Israeli Knesset passed Amendment No. 140 to the Income Tax Ordinance, according to which the corporate income-tax rate would be gradually reduced from 36% to 30% by 2007 (2004-35%, 2005-34%, 2006-32%, 2007-30%).

F. The Company and one of its subsidiaries are "Industrial Companies" as defined in the Israeli Law for the Encouragement of Industry (Taxes)-1969. Based on this Law, the Company and that subsidiary file consolidated tax returns.

G. The Company and its Israeli Subsidiaries possess final tax assessments through 2001.

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NOTE 23 - RELATED PARTIES AND INTERESTED PARTIES

A. Balances with Related Parties

	Consolidated		Company	
	----- December 31, -----			
	2 0 0 4	2 0 0 3	2 0 0 4	2 0 0 3
	----- Reported Amounts ----- NIS in thousands	----- Adjusted Amounts ----- NIS in thousands	----- Reported Amounts ----- NIS in thousands	----- Adjusted Amounts ----- NIS in thousands
Trade receivables (*)	1,373	554	18,731	8,354
Capital note - shareholder	32,770	32,770	32,770	32,770
Capital notes - Subsidiaries	-	-	4,205	4,205
	=====	=====	=====	=====

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Trade payables (*)	39,055	23,752	31,251	24,097
	=====	=====	=====	=====

(\*) Company - excludes Subsidiaries in Israel. See also Notes 4 and 11.

B. Transactions with Related Parties and Subsidiaries

	Consolidated			Company	
	Year ended December 31,			Year ended December 31,	
	2 0 0 4	2 0 0 3	2 0 0 2	2 0 0 4	2 0 0 3
	Reported	Adjusted	Adjusted	Reported	Adjusted
	Amounts	Amounts	Amounts	Amounts	Amounts
	-----	-----	-----	-----	-----
	NIS in thousands			NIS in thousands	
Sales to related parties	12,565	6,103	17,646	9,903	4,169
	=====	=====	=====	=====	=====
Sales to Subsidiaries	-	-	-	454,289	358,767
	=====	=====	=====	=====	=====
Cost of sales	162,096	169,469	224,682	58,254	61,703
	=====	=====	=====	=====	=====
Royalties	20,468	15,642	12,220	1,679	1,500
	=====	=====	=====	=====	=====
Other selling expenses (*)	-	-	2,413	-	-
	=====	=====	=====	=====	=====
General and administrative expenses (*)	8,969	8,201	7,380	1,878	1,428
	=====	=====	=====	=====	=====
Financing income, net (*)	-	3,314	2,076	2,784	2,526
	=====	=====	=====	=====	=====

(\*) Company - excludes Subsidiaries in Israel.

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NOTE 24 - DISCLOSURE AND PRESENTATION OF FINANCIAL INSTRUMENTS

A. Credit Risk

The revenues of the Group's principal Subsidiaries are derived from two major customers and a large number of smaller customers. Management regularly monitors the balance of trade receivables and the financial statements include an allowance for doubtful accounts based on management's estimation. Taking the aforementioned into consideration, the exposure to credit risk from trade receivables is immaterial.

Cash and cash equivalents and long-term deposits (including amounts in foreign currency) are deposited with major banks in Israel and abroad. Therefore, it is not expected that such banks will fail to meet their obligations.



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B. Fair Value of Financial Instruments

The financial instruments of the Group consist primarily of non-derivative assets and liabilities. Non-derivative assets include cash and cash equivalents, deposits, receivables and other current assets. Non-derivative liabilities include trade payables and other current liabilities. Due to the nature of these financial instruments, their fair value, generally, is identical or close to the value at which they are presented in the financial statements, unless stated otherwise.

Due to the fact that as of December 31, 2004, the terms of the capital note of shareholder do not include determined payment dates, fair value based on present values cannot be established. Accordingly, the fair value of the capital note is not disclosed in the financial statements.

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NOTE 25 - COMPANY'S FINANCIAL INFORMATION IN NOMINAL VALUES FOR TAX PURPOSES

A. Balance Sheets

	Com
	Dece
	2 0 0 4
	NIS in
Current Assets	
Cash and cash equivalents	109,717
Current maturities of long-term bank deposits	-
Trade receivables	113,448
Other receivables	12,360
Inventories	71,185
	-----
	306,710
Long-Term Investments	
Capital note of shareholder	32,770
Investments in Subsidiaries	169,303
	-----
	202,073
Fixed Assets, net	220,520
	-----
	729,303
Current Liabilities	
Short-term bank credit	-
Trade payables	265,546
Other payables and accrued expenses	12,249
	-----
	277,795
	-----

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Shareholders' Equity

451,508  
-----  
729,303  
=====

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NOTE 25 - COMPANY'S FINANCIAL INFORMATION IN NOMINAL VALUES FOR TAX PURPOSES (cont.)

B. Statement of Operations

	Year ended December 31,		
	2 0 0 4	2 0 0 3	2 0 0 2
	-----	-----	-----
	NIS in thousands		
Net sales	479,320	387,019	308,566
Cost of sales	392,376	334,764	245,936
	-----	-----	-----
Gross profit	86,944	52,255	62,630
Selling expenses	15,283	7,827	6,038
General and administrative expenses	4,985	4,327	5,762
	-----	-----	-----
Operating profit	66,676	40,101	50,830
Financing income (expenses), net	(4,541)	(5,995)	3,676
Other income, net	282	255	254
	-----	-----	-----
Income before income taxes	62,417	34,361	54,760
Income taxes	9,115	1,428	16,344
	-----	-----	-----
Income after income taxes	53,302	32,933	38,416
Equity in net earnings of Subsidiaries	16,660	29,682	8,881
	-----	-----	-----
Net income for the year	36,642	62,615	47,297
	=====	=====	=====

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NOTE 25 - COMPANY'S FINANCIAL INFORMATION IN NOMINAL VALUES FOR TAX PURPOSES (cont.)

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C. Statements of Changes in Shareholders' Equity

	Share capital -----	Capital reserves -----	Translation adjustments relating to foreign held autonomous Subsidiary -----	Retain earnin -----
	NIS in thousands			
Balance - January 1, 2002	8,263	132,127	-	206,97
Changes during 2002:				
Dividend declared after balance-sheet date				(35,52)
Exchange rate differences of prior year declared dividend				(2,53)
Net income for the year				47,29
Balance - December 31, 2002	8,263	132,127	-	216,20
Changes during 2003:				
Dividend paid				
Exchange rate differences of prior year declared dividend				(97)
Net income for the year				62,61
Balance - December 31, 2003	8,263	132,127	-	277,85
Changes during 2004:				
Dividend paid				
Distribution of bonus shares	250	23,615		(23,86)
Translation adjustments relating to foreign held autonomous Subsidiary			(3,377)	
Net income for the year				36,64
Balance - December 31, 2004	8,513	155,742	(3,377)	290,63
	=====	=====	=====	=====