# Azrieli Group Ltd.

Annual report 2018

# Azrieli Group Ltd.

## Periodic Report
As of December 31, 2018

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AZRIELI GROUP

# Description of the Corporation's Business

# Part A

# CHAPTER A | DESCRIPTION OF THE COMPANY'S BUSINESS

# FOREWORD AND GENERAL DEFINITIONS

Azrieli Group Ltd. hereby respectfully files the Description of the Corporation's Business Report as of December 31, 2018 (the "Report Date"), reviewing the Group and describing the development of business thereof, in 2018 (the "Report Period") until the Report Release Date. The Report is prepared pursuant to the provisions of Regulation 8a of the Securities Regulations (Periodic and Immediate Reports), 5730-1970. Figures appearing in the Report are true as of the Report Date. However, in certain cases details appear in the Report reviewing events which occurred subsequently to the Report Date until shortly before the date of release thereof, on March 20, 2019 (the "Report Release Date") and in such cases the Company notes that these are provided as of the relevant date.

Chapter A of the Report (this chapter) should be read together with its other parts, including the notes to the Financial Statements.

Materiality

The materiality of the information included in this Report, including a description of the material transactions and/or material projects, is evaluated from the point of view of the Company. It should be clarified that, in a part of the cases, the Company, in its exclusive discretion, decided to expand the description necessary, in order to give a more comprehensive picture of the subject being discussed.

Forward Looking Information

The description of the corporation's business in this Chapter A partly includes forward looking information as defined in the Securities Law. Such information which is presented below and indicated as forward looking information, includes forecasts, assessments, estimates or other information that is deemed as uncertain information which refers to a future event and which relies, inter alia, on publications of the Central Bureau of Statistics, Bank of Israel, other relevant professional entities and in addition, on internal estimates of the Company that are based on statistics, experience and information accumulated by the Company over the years. Actual results may materially differ from those forecasted in the context of the forward-looking information as aforesaid, as a result of a large number of factors, including as a result of the risk factors, in whole or in part, as described in Section 28 herein, all as will be specified in the specific references to forward looking information later in the chapter. Sentences which include expressions such as "expected", "intends", "estimates", "foresees", "expects" and similar expressions indicate that this is forward looking information. Such information reflects the Company's current point of view regarding future events that are based on estimates and therefore are subject to risk and uncertainty.

## DEFINITIONS

In this Chapter, the following terms shall bear the meaning stated alongside them:

| | |
|---|---|
| “TASE” | Tel Aviv Stock Exchange Ltd. |
| “Granite” or “Granite Hacarmel” | Granite Hacarmel Investments Ltd., a wholly-owned subsidiary of the Company |
| “Board of Directors’ Report” | The Company’s Board of Directors’ Report on the State of the Company's Affairs as of December 31, 2018, which is included as Chapter B of the Periodic Report |
| “Periodic Report” or “Report” | The Company’s periodic report for 2018 |
| “Financial Statements” | The consolidated financial statements of the Company as of December 31, 2018, which are included in Chapter C of the Periodic Report |
| “Company” | Azrieli Group Ltd. |
| “Companies Law” | The Companies Law, 5759-1999 |
| “Securities Law” | The Securities Law, 5728-1968 |
| “Leumi Card” | Leumi Card Ltd. |
| “Midroog” | Midroog Ltd. |
| “Ma’alot” | Standard & Poor’s Maalot Ltd. |
| “Nadav Investments” | Nadav Investments Inc., a private company incorporated under Canadian Law, fully owned and controlled by Azrieli Holdings |
| “Sonol” | Sonol Israel Ltd. |
| “Supergas” | Supergas Israeli Gas Distribution Company Ltd., a subsidiary wholly owned by Granite |
| “Azrieli E-Commerce” | Azrieli E-Commerce Ltd., a wholly-owned subsidiary of the Company |
| “Azrieli Holdings” | Azrieli Holdings Inc., a private company incorporated under Canadian Law, which is owned and controlled by Mmes. Sharon Azrieli, Naomi Azrieli and Danna Azrieli |
| “Granite Group” or “Granite Hacarmel Group” | Granite Hacarmel and/or subsidiaries thereof and/or affiliates thereof |
| “Azrieli Group” or “Group” | The Company and/or subsidiaries thereof and/or affiliates thereof including consolidated corporations |
| “Canit Hashalom” | Canit Hashalom Investments Ltd., a wholly owned subsidiary of the Company |
| “Azrieli Foundation (Israel)” | The Azrieli Foundation (Israel), R.A. 580503118, a not-for-profit association registered in Israel, acting, *inter alia*, to promote education and culture through projects in the fields of culture, welfare and science |
| “Azrieli Foundation (Canada)” | The Azrieli Foundation, a registered Canadian charitable foundation, incorporated and seated in Canada, whose assets are designated for donations and for the funding of philanthropic activities in Israel and in Canada, which is a stakeholder in the Company |

| | |
|---|---|
| "2017 Periodic Report" | The Company's annual periodic report for the year 2017, released by the Company on March 21, 2018 (Ref. 2018-01-027244), which is included herein by way of reference |
| "Prospectus" | A public offering prospectus published by the Company on May 12, 2010 as amended on May 12, 25 and 30, 2010 |
| "Shelf Prospectus" | A shelf prospectus released by the Company on May 10, 2016 bearing the date May 11, 2016. For details see the Company's immediate report of May 10, 2016 (Ref.: 2016-01-063049) which is included herein by way of reference |
| "GES" | G.E.S.- Global Environmental Solutions Ltd., a private company which was incorporated in Israel and is a wholly owned subsidiary of Granite |

# CHAPTER A | DESCRIPTION OF THE COMPANY'S BUSINESS

## PART ONE: DESCRIPTION OF THE GENERAL DEVELOPMENT OF THE COMPANY'S BUSINESS

## 1. The Company's operations and description of the development of its business

### 1.1 General

The Company was incorporated on January 6, 1983, as a private company according to the laws of the State of Israel. On June 3, 2010, the Company's shares were issued to the public for the first time and began to be traded on TASE on June 7, 2010, and the Company became a public company, within the meaning thereof in the Companies Law. Commencing from July 1, 2010, the shares of the Company are included in the Tel Aviv 35 Index (Formerly Tel Aviv 25 index). The Company's Series B and Series C bonds are included, *inter alia*, in the Tel Bond 40 Index, and the Company's Series D bonds are included, *inter alia*, in the Tel Bond 20 Index.

As of the Report Date, Mmes. Sharon Azrieli, Naomi Azrieli and Danna Azrieli are the controlling parties of the Company.[1]

As of the Report Date, the Company is engaged primarily in the various real estate segments, with most of the business operations of the Company being in the retail center and mall segment in Israel, in the office and other space for lease segment in Israel and abroad, and in the senior housing segment. The Company has an additional operating segment centralized under Granite Hacarmel, which is engaged through subsidiaries (Supergas and GES), in the marketing of alternative energy sources and industrial chemicals, wastewater, air, waste and water treatment (the "Granite Segment"). In addition, the Group has additional business of e-commerce and minority holdings in financial corporations, all as specified in Chapter A herein.

Until July 2016, the Company, through Granite, held Sonol. In view of the closing of the transaction for the sale of the Group's holdings in Sonol, the Sonol business has become discontinued operations. Until February 2019 the Company held 20% of Leumi Card. For details see Section 1.3.9 of this Chapter A below. In the long term, as previously reported by the Company, the Company intends to focus on the core areas of the real estate business and therefore examines, from time to time, its holdings in the non-real estate segments.

The Company owns income-producing properties in a total GLA of approx. 1,205 thousand sqm in addition to approx. 680 thousand sqm projects under development. The average occupancy rate in Israel is approx. 99%,[2] with 92% of the value of income-producing investment properties and income-producing properties under construction (consolidated) attributed to real estate in Israel.

Azrieli Group is the leading real estate group in Israel, was founded by Mr. David Azrieli OBM. In July 2014, Ms. Danna Azrieli, was appointed as Active Chairman of the Company's Board of Directors, after many years in which she served in key positions in the Group. The operations of the Group are carried out by means of a managerial headquarter that is comprised of professionals having a great deal of seniority and managerial experience, most of whom have been associated with the Company and the Group's companies for many years. The Company estimates that the Chairman of the Board, Ms. Danna Azrieli, as well as the experienced officers and managers in the Company who are considered professional and industry leaders, are principal and significant factors of the success of the Company's business results.

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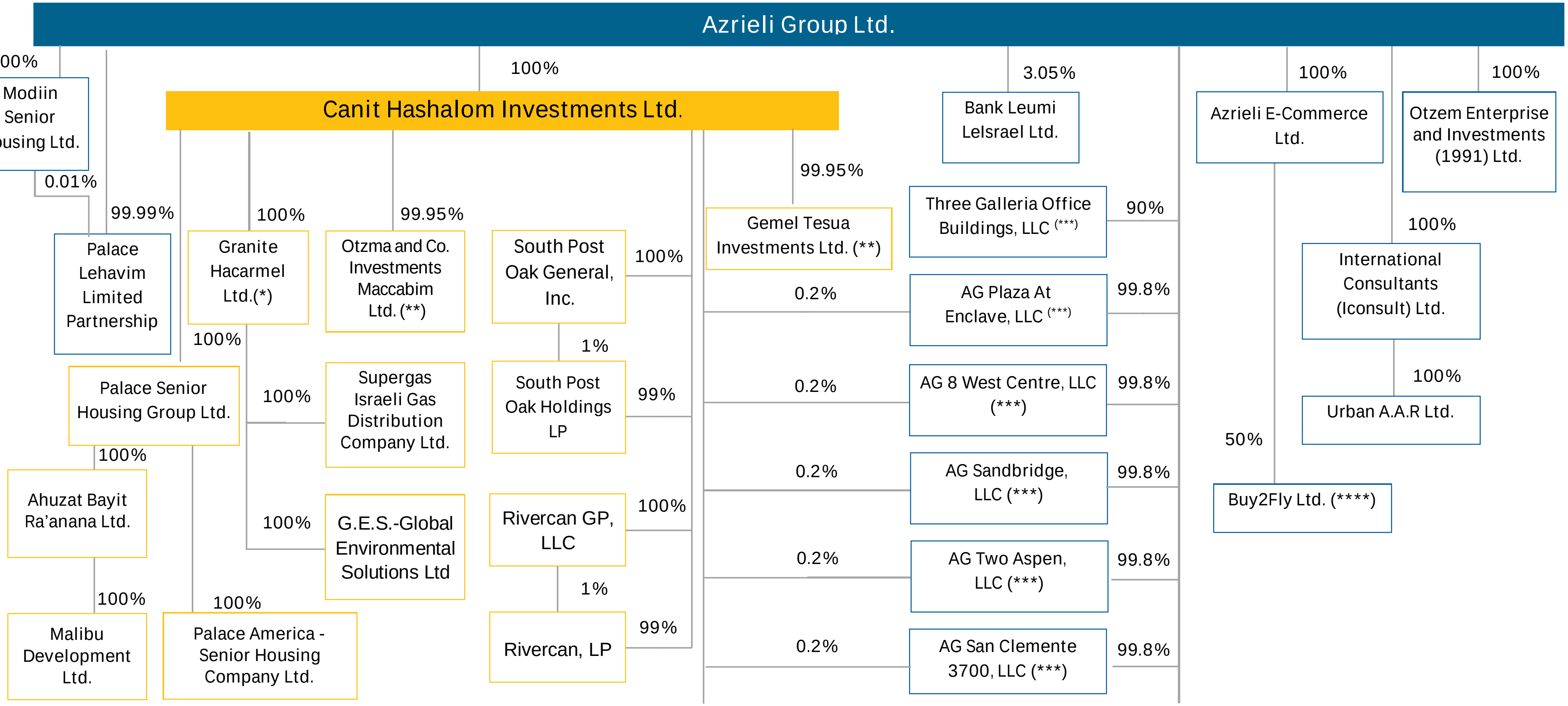
[1] For further details see immediate report on the status of holdings of interested parties and officers of April 10, 2018 (Ref.: 2018-01-036073), which is included herein by way of reference.

[2] Excluding the two buildings in Phase B in Holon Azrieli Center which opened at the end of 2015 and the end of Q1/2016 into which tenants are moving in as well as the offices in Rishonim and Sarona.

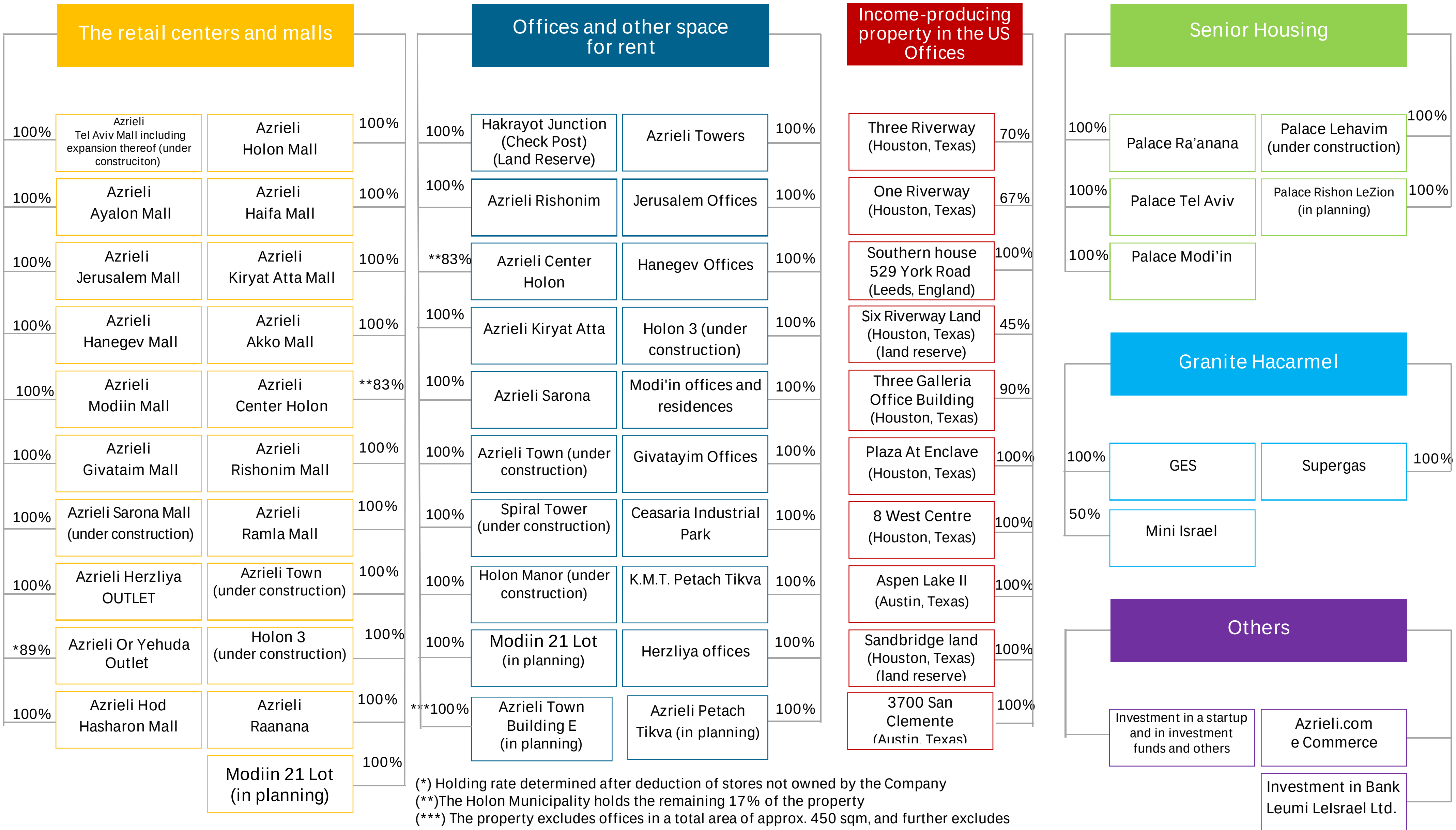
## 1.2 The Group's main holdings chart as of the Report Release Date*

### 1.2.1 Following is a chart updated as of the Report Release Date:




* Main holdings only. The chart does not include companies that are inactive as of the Report Release Date nor property management companies.
** 0.05% of these companies is held by International Consultants (iConsult) Ltd.
*** Indirectly, through companies and/or partnerships.
**** 50% by Gulliver Tourism Ltd.

### 1.2.2 As of the Report Release Date, the Group's asset holdings chart, in the final holdings structure, by operating segment, is as follows:




(*) Holding rate determined after deduction of stores not owned by the Company
(**)The Holon Municipality holds the remaining 17% of the property
(***) The property excludes offices in a total area of approx. 450 sqm, and further excludes a gas station and convenience store adjacent thereto.
(****) Mini Israel is held 50% by Granite and the remaining 50% by companies from the Shikun & Binui Group.

## 1.3 Summary of the main developments occurring in the Group's structure and business in 2018 and until the Report Release Date

### 1.3.1 Properties under construction

During the Report Period the Group continued to invest in the development and construction of new properties, and in the expansion and renovation of existing properties. For detail regarding the developments in the Group's properties under development during the Report Period, see Section 7.7 of Chapter A herein and Section 4.1 of the BOD report.

### 1.3.2 Changes in officers positions in the Company

Mr. Eyal Henkin was appointed as the Company's CEO, beginning January 1, 2018[3]. Prior to his appointment to this position, he was the ECO of Supergas for about eight years.

In August 2018 Ms. Rachel Mittelman was appointed as the Group's VP Information Systems, beginning September 2018.

In February 2019, Mr. Assaf Aviv was appointed as the Group's VP Innovation and Business Development, beginning March 2019.

### 1.3.3 Winning a tender for the purchase of land in Modi’in (lot 21)

On January 11, 2018, the Group won a tender held by the Israel Land Authority for the purchase of long-term lease rights in a lot located in the CBD of Modi'in-Maccabim-Reut, on an area of approx. 5,300 sqm, designated for the construction of 80 residential units, 50 hotel rooms, offices and retail, in consideration for approx. NIS 101.5 million. For further details, see the Company's immediate report of January 11, 2018 (Ref.: 2018-01-004960), which are included herein by way of reference.

### 1.3.4 Extension of the validity of the Shelf Prospectus

On March 21, 2018, the ISA extended the validity of the Shelf Prospectus by additional 12 months, i.e. until May 11, 2019. The Company shall file, concurrently to this report, a new draft prospectus to the ISA.

[3] For details regarding the conditions of office and employment of Mr. Henkin, as approved by the Company's shareholders general meeting of April 30, 2018, see Part B of the report on the convening of a meeting dated March 21, 2018 (Ref.:2018-01-027295) and immediate report on the results of the meeting dated May 1, 2018 (Ref.: 2018-01-043000), as well as Note 35C (6) of the Financial Statements. All of the information in the aforesaid reports is included herein by way of reference.

### 1.3.5 Engagement of Supergas Natural in an agreement with a third party for the purchase of natural gas

For details regarding the engagement of Supergas Natural in an agreement with a third party for the purchase of natural gas, see Note 29B(4) of the Financial Statements.

### 1.3.6 Winning a tender for the construction of waste sorting and recycling and energy production facility in the area of Rishon LeZion

On April 10, 2018, notice was received at Zero Waste Ltd. (“Zero Waste”), a corporation held by GES in equal shares with Shikun & Binui Ltd. ("Shikun & Binui"), whereby Zero Waste was elected as the winner in a BOT tender for the planning, financing, construction and operation of a municipal waste sorting and recycling and energy production facility (the “Project”), published by the Ministry of Finance (the Accountant General) and the Ministry of Environment Protection. The Project will be built in the area of the Dan Region Wastewater Treatment Plant (the “*Shafdan*”) in Rishon LeZion, and its cost during the construction period is estimated at approx. NIS 750 million. The performance of the Project is subject to completion of a financial closing of the Project. For further details see Note 29B(7) to the Financial Statements and the Company's immediate report of April 11, 2018 (Ref.: 2018-01-036841), which is incorporated herein by way of reference.

On July 2, 2018, the Company updated that Zero Waste has received the petition of another group which contended in the same tender, in which the Jerusalem District Court is moved, *inter alia*, to order the cancellation of the decision of the tender committee to elect Zero Waste as the winner of the tender and rule that the other group is the winner thereof, and alternatively to order to remand the discussion to the tender committee, for a review of the compliance of Zero Waste with the tender requirements. On February 14, 2019, the Court’s decision was given, denying the petition with no award of costs. For further details, see the Company's immediate reports of July 2, 2018 (Ref.: 2018-01-058617) and February 14, 2019 (Ref.: 2019-01-013639), which are included herein by way of reference.

### 1.3.7 Engagement in an agreement for the purchase of rights to land located on Menachem Begin Road Tel Aviv (Azrieli Town E)

On April 22, 2018, the Company entered into an agreement with unrelated third parties (the “Sellers”) for the purchase of rights to land located on Menachem Begin Road, Tel Aviv, holding a 4-floor building over a commercial ground floor, in the total area of approx. 5,500 sqm, mostly leased for office purposes and underground floors. The property includes unused building rights under the zoning plan that applies to the land, in the total scope of approx. 21,000 sqm above-ground, as well as additional rights. In consideration for the purchase of rights to the land, the Company paid the Sellers NIS 260 million (exclusive of V.A.T.). The transaction was closed on May 14, 2018. For further details, see the Company's immediate reports of April 23, 2018 and May 14, 2018 (Ref.: 2018-01-040060 and 2018-01-038517, respectively), which are included herein by way of reference.

### 1.3.8 Sale of land in Pi Glilot

On May 10, 2016, the Company and Granite, including through Sonol, sold to third parties all of their holdings of land in Pi Glilot and shares in Pi Glilot (which holds the long-term leasehold on land in the Pi Glilot complex), for a total consideration of approx. NIS 130 million. During the Report Period, the transactions have been consummated and the consideration therefor has been paid in accordance with the provisions of the sale agreements.

### 1.3.9 Sale of the Company's holdings in Leumi Card

In July 2018, the Company engaged, together with Bank Leumi LeIsrael Ltd. (in this section: the "Bank" and jointly the "Sellers"), in an agreement (in this section: the "Agreement") for the sale of all of the Sellers' holdings in Leumi Card to Warburg Pincus Financial Holdings (Israel) Ltd., a corporation controlled by the Warburg Pincus investment fund (the "Buyer"). In consideration for the purchase of all of the Seller's shares in Leumi Card, the Buyer shall pay the Sellers a sum of NIS 2,500 million (subject to adjustments) in three installments at different rates, according to the dates fixed in the Agreement. The Company's share in the consideration is NIS 500 million (subject to adjustments). The Agreement includes provisions regarding collateral, which the Buyer is obligated to provide to the Sellers as well as representations and indemnity provisions, specified in the Agreement. The Agreement also includes several conditions precedent, including the receipt of the regulatory approvals for the transaction that are required by law. On December 2, 2018, the Anti-Trust Commissioner's approval for the performance of the said transaction was received. On February 25, 2019, the transaction was closed and the consideration for this stage was received according to the provisions of the Agreement. For further details, see the Company's immediate reports of July 28, 2018, October 29, 2018, December 3, 2018, February 4, 2019, February 14, 2019 and February 25, 2019 (Ref.: 2018-01-069771, 2018-01-1001721, 2018-01-117489, 2019-01-012261, 2019-01-013513 and 2019-01-016348, respectively), which are included herein by way of reference.

### 1.3.10 Closing of the acquisition of an office building in Austin, Texas, U.S.A.

In July 2018, the Group closed the acquisition of an office building in Austin, Texas, U.S. in consideration for approx. U.S. $100.4 million (including transaction costs). For further details see Section 10.9 of Chapter A herein.

### 1.3.11 Income tax assessments

On December 12, 2018, a settlement agreement was signed between the Company and Canit Hashalom Investments Ltd., a wholly-owned subsidiary of the Company, with the Israel Tax Authority in respect of tax assessments pursuant to Section 152(B) of the Income Tax Ordinance [New Version] for the years 2011-2014, with respect to which the Company filed an appeal with the Court, and also in respect of the years 2015-2016 (the "Settlement Agreement"). According to the Settlement Agreement, the Company paid amounts, most of which will be returned to the Company in the coming years as a deduction from future tax liability (timing differences). The Settlement Agreement did not have a material effect on the Company's financial results. For further details, see Note 28F to the financial statements and the Company's immediate reports of December 12, 2018, January 2, 2018 and December 6, 2016 (Ref.: 2018-01-121545, 2018-01-000994 and 2016-01-136948, respectively), which are incorporated herein by way of reference.

### 1.3.12 Financing transactions[4]

In February 2018 the Company expanded the Company's Bond Series D, such that additional Bond series D were allotted, of approx. NIS 1,367 million par value, in consideration for approx. NIS 1,409 million (approx. NIS 1,400 million net of the issue expenses).

For further details regarding the expansion of the Bond Series D and the issue of Bond Series E and F as aforesaid, see Section 19.5 of Chapter A herein.

After the Report Period, on January 22, 2019, the Company issued two new bond series of the Company (Bond Series E and F), such that Series E Bonds of approx. NIS 1,215,959,000 par value were allotted in consideration for approx. NIS 1,215,959,000 (approx. NIS 1,207 million net of the issue expenses), and Bonds Series F of approx. NIS 263,383,000 par value were allotted in consideration for the amount of approx. NIS 263,383,000 million

[4] Pursuant to the Shelf Offering Report published on January 31, 2018 (Ref.: 2018-01-010993) that was published under a shelf prospectus. The said report is included herein by way of reference.

(approx. NIS 260 million, net of the issue expenses). The total proceeds received by the Company under the issue of both these series totaled approx. NIS 1,479 million (gross of the issue expenses).

## 2. Main operating segments of the Group

As of the Report Date, the Company reports to the public on five operating segments[5]:

1. The retail centers and malls in Israel segment: In this operating segment, the Group focuses, primarily, on promoting, constructing, acquiring, renting, managing and maintaining malls and retail centers in Israel. As of the Report Date, the Group owns 17 malls and retail centers in Israel, in a total leasable area of approx. 335 thousand sqm leased (on a consolidated basis and the Company's share) to some 1,900 tenants, with most of the malls and retail centers spread throughout the large cities in Israel. In the framework of this operating segment, the Company provides management services to the retail centers and malls maintained thereby, with the management being performed by the Company and/or designated management companies for each mall or retail center that is owned by the Group, and enters into management agreements with the tenants. All of the malls and retail centers also include car parks (above or underground) which serve the visitors and the tenants. See Section 8 of Chapter A herein for additional details regarding the retail centers and malls segment.

2. The office and other space for lease segment in Israel: In this operating segment, the Company primarily engages with promoting, constructing, acquiring, renting, managing and maintaining office buildings and parks for offices and high-tech industry, logistic areas and storage in Israel. As of the Report Date, the Group owns 14 income-producing properties in the office and other space for lease segment in Israel, in a total leasable area of approx. 548 thousand sqm (on a consolidated basis and the Company's share) that are leased to about 650 tenants. Most of the Group's income-producing areas in this operating segment are located in projects which integrate commercial areas. See Section 9 of Chapter A herein for additional details regarding the office and other space for lease segment in Israel.

3. The income-producing property segment in the U.S.: As of the Report Date, the Group owns 8 office properties for lease outside of Israel, in a total leasable area of approx. 246 thousand sqm (the Company's share is approx. 236 thousand sqm) that are leased to some 250 tenants. See Section 10 of Chapter A herein for additional details with respect to the income-producing property segment in the U.S.

4. The senior housing segment: The Company has three active senior homes in an aboveground built-up area of approx. 76 thousand sqm (excluding areas which are attributed to the LTC unit and to retail areas), which comprise approx. 800 senior housing units, and two projects under development and construction for approx. 600 residential units in a total area of approx. 60 thousand sqm (excluding areas which are attributed to the LTC unit and to retail areas). For further details about the senior housing segment, see Section 11 of Chapter A herein.

[5] In view of the closing of the transaction for the sale of the Group's holdings in Sonol, as of the quarterly statement for June 30, 2016, Sonol's operations have become discontinued operations, in accordance with GAAP, and it is presented in the Company's income statements separately from the continuing operations (see Note 8 to the Financial Statements). In view of the aforesaid, as of the statement for Q3/2016, the Company has begun reporting its operations in the Granite Segment as a separate operating segment, within the definition of such term in GAAP. Furthermore, as of the statement for Q3/2016, the Company's operations in the senior housing segment are being described as a separate operating segment, in view of the establishment and expansion of the operations and investment in projects under development in this segment.

5. The Granite Segment: The Company holds (through Granite Hacarmel) 100% of the rights in Supergas, which engages in the marketing of alternative energy sources and 100% (through Granite Hacarmel) of GES, which is engaged in chemicals for industry, wastewater, air, waste and water treatment. For further details about the Granite Segment, see Section 12 of Chapter A herein.

Other assets and business:

For details on other assets and business which is not included in the operation segments described above, including e-Commerce activity, investments in banking and financial corporations and investments in investment funds, see Section 14 of Chapter A herein.

## 3. Investments in the Company's capital and transactions in its shares

To the best of the Company's knowledge, no investments have been made in the Company's capital over the past two years and no other material transaction has been executed in the Company's shares by an interested party outside of the TASE during the two years preceding December 31, 2018, as well as until this Report Release Date, except as specified below:

| Subject of the Report | Report Release Date | Reference[6] |
|---|---|---|
| Changes that occurred in the holdings of Mr. Menachem Einan, a director of the Company | January 1, 2017 | 2017-01-000042 |
| Changes that occurred in the holdings of Mr. Joseph Ciechanover, a director of the Company | April 30, 2017 | 2017-01-043860 |
| Changes that occurred in the holdings of Migdal Insurance and Financial Holdings Ltd. holdings, which ceased being an interested party in the Company | June 6, 2017 | 2017-01-057501 |

For details on the status of holdings of interested parties in the Company see immediate report of April 10, 2018 (Ref.: 2018-01-036073), which is included herein by way of reference.

## 4. Dividend Distribution

### 4.1 Following are details on the dividend distribution in 2017, 2018 and 2019 (until the Report Release Date):

| Resolution Date | Distribution Date | Dividend Amount per Share (NIS) | Resolution Date |
|---|---|---|---|
| March 21, 2017 | May 10, 2017 | 3.9580 | 480 |
| March 20, 2018 | May 2, 2018 | 4.28 | 520 |
| March 19, 2019 | May 6, 2019 | 4.62 | 560 |

(a) The above-specified distributions did not require obtaining a court approval.

(b) The Company's retained earnings available for distribution as of December 31, 2018 are approx. NIS 13.9 billion (such retained earnings also include property revaluation profits).

(c) For further details on the dividend distribution in the Company and a dividend distribution limitation, see Notes 21B-C and 19B(1) to the financial statements.

[6] All of the reports in this section below are included herein by way of reference.

## 5. Financial information regarding the Company's operating segments

The following presents financial data of the Company, as specified in the Company's financial statements (NIS in millions) for the years 2016 to 2018:

### Y2018:

| | Retail centers and `Israel | Office and other space for lease in Israel | Income-producing property in the U.S. | Senior housing | Granite | Adjustments* | Consolidated |
|---|---|---|---|---|---|---|---|
| | NIS in millions | NIS in millions | NIS in millions | NIS in millions | NIS in millions | NIS in millions | NIS in millions |
| Revenues | | | | | | | |
| Total revenues from outsiders | **1,034** | 633 | 267 | 130 | 720 | 37 | 2,821 |
| Total revenues from other Group operating segments | - | - | - | - | - | - | - |
| Total | 1,034 | 632 | 267 | 130 | 720 | 37 | 2,821 |
| Attributed costs | | | | | | | |
| Costs not representing revenues from other Group operating segments | 214 | 116 | 118 | 93 | 603 | 90 | 1,234 |
| Costs representing revenues of other Group operating segments | - | - | - | - | - | - | - |
| Total | 214 | 116 | 118 | 93 | 603 | 90 | 1,234 |
| Income from operations attributed to operating segment (NOI in the income-producing real estate segments) | 820 | 517 | 149 | 37 | 117 | (53) | 1,587 |
| Variable costs attributed to the operating segment | 199 | 108 | 69 | 86 | 405 | 39 | 906 |
| Fixed costs attributed to the operating segment | 15 | 8 | 49 | 7 | 198 | 51 | 328 |
| Increase (decrease) in the fair value of investment property | (4) | 167 | (48) | 103 | - | - | 218 |
| Income from operations attributable to the shareholders of the parent company | 820 | 517 | 144 | 37 | 117 | (53) | 1,582 |
| Income from operations attributable to non-controlling interests | - | - | 5 | - | - | - | 5 |
| Total assets attributed to the operating segment | 12,682 | 10,443 | 2,593 | 2,081 | 1,225 | - | 29,024 |

*Adjustments to the consolidated basis derive mainly from business in the e-Commerce segment – for details see Section 14 of Chapter A herein.

## Y2017:

| | Retail centers and `Israel | Office and other space for lease in Israel | Income-producing property in the U.S. | Senior housing | Granite | Adjustments* | Consolidated |
|---|---|---|---|---|---|---|---|
| | NIS in millions | NIS in millions | NIS in millions | NIS in millions | NIS in millions | NIS in millions | NIS in millions |
| Revenues | | | | | | | |
| Total revenues from outsiders | 1,032 | 489 | 221 | 126 | 705 | 19 | 2,592 |
| Total revenues from other Group operating segments | - | - | - | - | - | - | - |
| Total | 1,032 | 489 | 221 | 126 | 705 | 19 | 2,592 |
| Attributed costs | | | | | | | |
| Costs not representing revenues from other Group operating segments | 204 | 92 | 100 | 87 | 601 | 65 | 1,149 |
| Costs representing revenues of other Group operating segments | - | - | - | - | - | - | - |
| Total | 204 | 92 | 100 | 87 | 601 | 65 | 1,149 |
| Income from operations attributed to operating segment (NOI in the income-producing real estate segments) | 828 | 397 | 121 | 39 | 104 | (46) | 1,443 |
| Variable costs attributed to the operating segment | 204 | 92 | 100 | - | 403 | 19 | 818 |
| Fixed costs attributed to the operating segment | - | - | - | 87 | 198 | 46 | 331 |
| Increase (decrease) in the fair value of investment property | (25) | 630 | (186) | 81 | - | - | 500 |
| Income from operations attributable to the shareholders of the parent company | 828 | 397 | 117 | 39 | 104 | (46) | 1,439 |
| Income from operations attributable to non-controlling interests | - | - | 4 | - | - | - | 4 |
| Total assets attributed to the operating segment | 12,368 | 9,462 | 1,983 | 1,725 | 1,265 | - | 26,803 |

*Adjustments to the consolidated basis derive mainly from business in the e-Commerce segment – for details see Section 14 of Chapter A herein.

## Y2016:

| | Retail centers and malls in Israel | Office and other space for lease in Israel | Income-producing property in the U.S. | Senior housing | Granite | Adjustments* | Consolidated |
|---|---|---|---|---|---|---|---|
| | NIS in millions | NIS in millions | NIS in millions | NIS in millions | NIS in millions | NIS in millions | NIS in millions |
| Revenues | | | | | | | |
| Total revenues from outsiders | 974 | 447 | 229 | 95 | 653 | 7 | 2,405 |
| Total revenues from other Group operating segments | - | - | - | - | - | - | - |
| Total | 974 | 447 | 229 | 95 | 653 | 7 | 2,405 |
| Attributed costs | | | | | | | |
| Costs not representing revenues from other Group operating segments | 195 | 78 | 105 | 66 | 570 | 12 | 1,026 |
| Costs representing revenues of other Group operating segments | - | - | - | - | - | - | - |
| Total | 195 | 78 | 105 | 66 | 570 | 12 | 1,026 |
| Income from operations attributed to operating segment (NOI in the income-producing real estate segments) | 779 | 369 | 124 | 29 | 83 | (5) | 1,379 |
| Variable costs attributed to the operating segment | 195 | 78 | 105 | - | 374 | 5 | 757 |
| Fixed costs attributed to the operating segment | - | - | - | 66 | 196 | 7 | 269 |
| Increase (decrease) in the fair value of investment property | 220 | 517 | (82) | 56 | - | - | 711 |
| Income from operations attributable to the shareholders of the parent company | 779 | 369 | 119 | 29 | 83 | (5) | 1,374 |
| Income from operations attributable to non-controlling interests | - | - | 5 | - | - | - | 5 |
| Total assets attributed to the operating segment | 12,074 | 8,219 | 2,176 | 1,495 | 1,298 | - | 25,262 |

*Adjustments to the consolidated basis derive from insurance operations and the e-Commerce. For details see Section 14 of Chapter A herein.

For explanations by the board of directors with respect to the financial data of the Company as included in its consolidated financial statements, see the Board of Directors' Report.

# 6. General environment and the effect of external factors on the Company's business

Following are the assessments of the Company as to the major trends, events and developments in the macroeconomic environment of the Company, which to the best of its knowledge and estimates, have or are anticipated to have material effect on the business results or the developments in the Group's operating segments. For details with respect to regulatory restrictions on the Company, see Section 23 of Chapter A herein.

The estimates of the Company below in this section and in this Report are based, *inter alia*, on data published by third parties and not independently examined by the Company. Every reference appearing in this section should be considered data not under the control of the Company and uncertain, and the said estimates are based, *inter alia*, on data published by the Bank of Israel, as specified below.

## 6.1 The business in Israel

As a company operating in the Israeli market, with its various industries, the Company is exposed to macro-economic changes in the condition of the economy in general and in the income-producing real estate industry, in particular. The central economic factors affecting the business of the Company and the Group companies in Israel are specified below.

| Israel | For the Year Ended on | | |
|---|---|---|---|
| | Dec. 31, 2018 | Dec. 31, 2017 | Dec. 31, 2016 |
| Macroeconomic parameters * | | | |
| Gross Domestic Product (PPP)* | $336.1 billion | $317.1 billion | $301.2 billion |
| Product per Capita (PPP)* | $37,856 | $36,405 | $35,260 |
| Growth rate in the Domestic Product (PPP)* | 6% | 5.25% | 5.1% |
| Growth Rate in the Product per Capita (PPP)* | 3.98% | 3.24% | 3.04% |
| Inflation Rate ** | 0.8% | 0.4% | (0.2)% |
| Return on long term domestic governmental debt *** (NIS) | 2.3% | 1.7% | 2.2% |
| Rating of long term governmental debt (international rating) **** | AA-/STABLE | A+/POSITIVE | A+/STABLE |
| Exchange Rate of domestic currency compared to the Dollar as of the last day of the year** | 3.748 | 3.467 | 3.845 |

* Source: the International Monetary Fund website – www.imf.org - World Economic Outlook Database The figures for 2018 are based on a forecast of October 2018 and are stated in current prices.
** Source: the Central Bureau of Statistics: www.cbs.gov.il
*** Source: yield on government debt, the Bank of Israel website: www.boi.org.il, yield-to-maturity on unlinked fixed-interest 10-year bonds (gross). The figures for 2018 are based on a publication of January 2019.
**** Source: S&P rating report at www.standardandpoors.com, as of January 2019.

### 6.1.1 General

1. Political-security situation – The Company's business is affected by the political-security situation in Israel. The Company's management estimates that significant and long-term deterioration in the political security situation may cause a decline in the business in malls and retail centers, decline in demands and a decrease in prices in the income-producing property segment.

2. Credit availability and cost – Changes in financing cost and availability and the scope of available credit in the banking and non-banking system affect the real estate industry and the profitability thereof. As a result of the implementation of structural reforms implemented in recent years in the capital market (such as the

Bachar Reform, the pension reform and the tax reform), the share of bank credit out of the total credit to the business sector is declining and a non-banking credit market has developed, constituting an alternative for financing assets and projects. The local capital market too, constitutes a source for the raising of funds to finance the Company's business activity, by way of issuing bonds, and also presently serves as the Company's primary source of financing.

Thanks to the financial strength of the Company, its accessibility to sources of bank financing, and the relatively low scope of pledges on properties, taking into consideration the extent of business thereof, the Company estimates that no difficulties are anticipated in raising the financing required thereby.

3. Fluctuations in the inflation rate, the Consumer Price Index and the interest rates – The real estate industry is exposed to risks deriving from changes in the interest rates, inflation rate and in the Consumer Price Index (CPI). The Company finances most of its business operations by means of loans linked to the CPI. In addition, most of the Company's revenues from rent are also linked to the CPI. The (known) CPI increased in 2018 by 1.2%, compared with an increase of 0.3% in the course of 2017. At the end of 2018, inflation expectations for the capital market in 2019 were at a rate of 1.2%, and the deriving expectations from the banks' internal interest rates were at a rate of 0.9%[7]. At the end of 2018, the Prime interest rate was 1.75%, in comparison with 1.60% at the end of 2017. The Bank of Israel interest rate increased at the end of 2018 to 0.25%, compared with a rate of 0.1% in 2017.[8]

4. Fluctuations in the exchange rate of the U.S. dollar – The Company has real estate properties in the U.S. at a scope of approx. 9% from the Group's total real estate properties. These properties were financed by loans linked to the U.S. Dollar. The change in the exchange rate of the U.S. Dollar has an effect on the difference between the real estate properties' value and the loans therefrom. In 2018, the Dollar strengthened against the Shekel, from an exchange rate of NIS 3.467 per Dollar at the end of 2017 to an exchange rate of NIS 3.748 per Dollar at the end of 2018.

### 6.1.2 Effects on the income-producing property in Israel segment

1. The income-producing property in Israel segment – For a description of the trends related to the income-producing property in Israel segment, in relation to each of the Company's business segments, see Sections 8.1, 9.1 and 11.1 of Chapter A herein.

2. The rate of growth and consumption per capita in Israel - In real terms, the growth of the Israeli economy continues in 2018, and the real activity indicates that growth will continue in the upcoming years. The gross domestic product (GDP) increased by approx. 3.3% in 2018, compared with 3.5% in 2017. In addition, a high level of employment was maintained and the unemployment rate continued to decline down to an annual average of approx. 4% (4.3% in Q4/2018)[9]. This year, private consumption expenditure grew by 3.9%, following an increase of 3% in 2017. Private consumption expenditure per capita in 2018 increased by 1.9%. According to publications of the Bank of Israel, the macroeconomic forecast was updated in January 2019, and according thereto the GDP is expected to grow to approx. 3.4% in 2019 and approx. 3.5% in 2020. Forecasts by the International Monetary Fund also predict that, in the next two years, Israel's product will grow by approx. 3% per year (in local currency values). The growth forecast in Israel derives also from domestic factors including strong domestic consumption, increase in investments and performance and also from factors in the global economy including rapidly growing global trade, the low interest rate environment, changes in the U.S. taxation policy and the bull capital market.

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[7] Bank of Israel, press release, January 20, 2019, the expectations for inflation from the various sources. The Bank of Israel website: http://www.boi.org.il/he/NewsAndPublications/PressReleases/Pages/200119.aspx.
[8] Bank of Israel, press release, January 7, 2019, the Monetary Committee decided to leave the interest for February 2019 unchanged, at the level of 0.25%, the Bank of Israel website: https://www.boi.org.il/he/NewsAndPublications/PressReleases/Pages/07-1-2019InterestRate.aspx.
[9] CBS – data from manpower survey of January 2019.

### 6.1.3 Data which may affect the results of the Granite Segment

The results of the Granite Segment are mainly exposed to the following effects: (1) changes in fuel prices, which affect the demand for Supergas' LPG and natural gas products; (2) effects of the competition in the alternative energy sources' market, which might adversely affect the business of Supergas, including a decrease in profit rates and the loss of market share; (3) regulatory changes applying from time to time to the operations of the Granite Segment, which might affect the businesses of the Segment, its financial position and the business results of the Granite Segment; (4) dependency on refineries, which are the main LPG supplier and on the Tamar gas reservoir, which is Supergas' only natural gas supplier; (5) since the companies in the Granite Segment (Supergas and GES) are engaged in operations that are subject to environmental regulation, including regulation concerning the segment of treatment, production and use of water, wastewater and hazardous and toxic substances, they are exposed to damage that might be caused due to such products or due to failures and malfunctions in such operations.

## 6.2 The business in the U.S.

| U.S. | For the Year Ended on | | |
|---|---|---|---|
| | Dec. 31, 2018 | Dec. 31, 2017 | Dec. 31, 2016 |
| Macroeconomic parameters | | | |
| Gross Domestic Product (PPP) (1) (U.S. $ in billions) | 20,513 | 19,485 | 18,707 |
| Product per Capita (PPP) (1) (U.S. $) | 62,518 | 59,792 | 57,815 |
| Growth rate in the Domestic Product (PPP) (1) | 5.27% | 4.16% | 2.68% |
| Growth Rate in the Product per Capita (PPP) (1) | 4.56% | 3.42% | 1.93% |
| Inflation Rate (2) | 1.9% | 2.1% | 2.1% |
| Return on long term domestic governmental debt (3) | 2.69% | 2.4% | 2.45% |
| Rating of long term governmental debt (4) | AA+/Stable | AA+/Stable | AA+/Stable |
| Exchange Rate New Shekel to U.S. Dollar (5) | 3.748 | 3.467 | 3.845 |

(1) The product data is based on a publication by the International Monetary Fund in October 2018 (www.imf.org).
(2) According to publications by the U.S. Department of Labor.
(3) According to the U.S. Department of Treasury with respect to bonds for a period of 10 years from December 31, 2018.
(4) According to the rating by S&P (www.standardandpoors.com).
(5) According to Bank of Israel data.

The Company's business in the U.S. is primarily affected by the economic situation in the U.S. economy in general, and in the income-producing commercial real estate sector in particular, the demand and supply in the area in which the Company's properties are located and the amount of rent therefor. In the course of 2018, the Federal Reserve raised the interest rate four times. To the best of the Company's knowledge, similarly to recent years, the U.S. economy continued to generate favorable positive economic figures also in 2018. In Q4/2018 the U.S. economy grew at an annual rate of 2.7%, following an annual growth rate of 3.5% in the three months preceding this quarter. In the entire year of 2018, growth rate was 2.9%, which is higher than the 2.2% rate of 2017. For details with respect to the Houston Texas area, where, as of the Report Date, the majority of the Company's business in the income-producing property in the U.S. segment is situated, see Section 10 of Chapter A herein.

*The above information in Sections 6.1 and 6.2 concerning the general environment and the external factors that affect the Company's business, includes information based on subjective estimates and approximations of the Company, which is forward-looking information, as defined in the Securities Law. The Company's estimations are in consideration of past experience, as well as publications and surveys written by professionals in connection with the condition of the Israeli economy, the real estate sector, the Granite Segment and the senior housing segment, and the condition of the economy in countries in which the Company operates, as detailed above in this section. The above data are only approximations and it is possible that they are incomplete, but, in the Company's estimation, are able to provide a general picture, even if inexact, of the markets in which it operates in the various operating segments.*

*In view of the above, and due to the existence of causes beyond the control of the Company, the actual results may vary from the estimates specified above if a change should take place in one of the factors which were taken into account in these estimates, the condition of the political and/or economic and/or security situation shall become worse or due to the realization of any of the risk factors specified in Section 28 of Chapter A herein, and mainly a global financial crisis, the condition of the economy in Israel and in the U.S. and the security situation in Israel, changes in relevant interest rates and indices, decline in demand for space for lease and in rent prices, deterioration of strength of primary tenants, and the costs of financing sources.*

# PART THREE: DESCRIPTION OF THE GROUP'S BUSINESS IN THE INVESTMENT PROPERTY SEGMENT – AGGREGATE

## 7. Aggregate disclosure with respect to the investment property segment[10]

The disclosure with respect to the Company's investment property operating segment is made in accordance with the draft of the amendment to the Securities Regulations (Details of the Prospectus and the Draft Prospectus – Structure and Form) (Amendment), 5764-2013, as released by the ISA in December 2013 (the "Disclosure Provision"), which had been adopted by the Company even prior to the entering into effect of the same.

### 7.1 General

The Group began its activity in the investment property segment in 1983. Since then and as of the Report Release Date, the Company operates in development, construction, acquisition, lease, management and maintenance of malls and retail centers in Israel as well as office and hi-tech parks, office and industry, light industry and storage buildings in Israel. Commencing from 2001 the Group began to operate also overseas (in particular in the U.S.) mostly in the office for lease segment and since 2014 the Group began developing also the senior housing segment.

As a development company, the Company examines, from time to time, growth and increase goals for the expansion of its scope of operations, and checks opportunities to purchase income-producing properties and lands for real estate development in Israel and overseas in the core segments thereof (retail and office spaces) and also in tangential segments such as senior housing and more. Underlying the Company's policy is the basic assumption whereby the property's location is the most important factor for its success. Accordingly, upon examination of the location of a potential property, the Company ascribes significant weight to the population growth potential in the examined area and the urban development anticipated therein, based, *inter alia*, on urban research, segmentation of the population, competition in the area and the unique or typical commercial needs of such area.

The Group's strategy and business in the investment property segment is performed both through initiation, development and construction of new properties and acquisition of existing income-producing property, upgrading the same and maximizing potential thereof. In the Report Period, the margins between the rates of capitalization on the properties and the financing costs remained high relative to previous periods, a trend which the Company estimates allows it to develop and purchase income-producing properties also at development yields or cap rates for purchase that are lower compared to rates in previous periods.

The Group, by itself (through companies which are entirely controlled thereby), manages and operates the properties in Israel, their construction and betterment while using the know-how and experience accrued by the Group, in order to give added value to its properties, tenants and the public visiting the properties.

The Company's properties in the retail centers and malls segment are located in the center of residential neighborhoods and at entrances to urban areas, insofar as possible, on main traffic arteries. Due to the location of the properties, their accessibility, spacious car parks, tenant mix and variety of activities therein, they attract a large and diverse target audience. Some of the retail centers include office space for lease designated to provide a supplementary response for the target audience's needs, according to the nature of the retail center and its location.

The Company's properties in the office and other space for lease in Israel segment, including the properties under construction, are located primarily in the central region (where there is an active demand for office buildings of various types) in proximity to central transport arteries and are characterized by a high standard of finishing and management, relatively large floor and office areas, and include designated parking.

According to its policy for the maximization of its profits and in order to improve the experience of the users of the Group's properties, the Company acts, as necessary, to upgrade its existing properties, while using the existing and potential commercial, office and other areas, improving the tenant mix and adjusting the same to the target audience, renovating the properties, renewing the systems therein and implementing technological and/or digital improvements.

[10] Disclosure is made jointly for the retail centers and malls in Israel segment, the office and other space for lease in Israel segment and the income-producing property in the U.S. segment and the Group's senior housing segment.

As previously reported by the Company, the Company examines, from time to time, the expansion of its operations, including entry into close real estate segments. Thus, in 2014, the Company began developing the senior housing business, upon the purchase of senior housing land in the city of Modi'in. As of the Report Release Date, the Company has three active senior homes: Palace Tel Aviv, which was acquired in 2015, Palace Ra'anana (formerly Ahuzat Bayit Ra'anana), the acquisition of which was closed in Q2/2016 and a senior home in Modi'in, which construction was completed during the Report Period, and occupation began in October 2018. The Company also has one additional project under construction in Lehavim, Stage A of which is scheduled to be opened in 2020. An additional Company project, in the city of Rishon LeZion, is in planning.

Set forth below are aggregate figures regarding investment property owned by the Group. The figures will be presented jointly with regard to properties from the four operating segments of investment property owned by the Company, namely: the retail centers and malls in Israel segment, the office and other space for lease segment in Israel, the overseas income-producing property segment and the senior housing segment in Israel. For further details regarding the operating segments and regarding material properties, see Sections 8, 9, 10 and 11 of Chapter A of the Report.

For details on land reserves, see Section 7.8 of Chapter A herein.

## 7.2 Summary results in the investment property segments*

### 7.2.1 Summary of the aggregate results in the Group's four investment property segments

| | For the year ended on | | |
|---|---|---|---|
| | Dec. 31, 2018 | Dec. 31, 2017 | Dec. 31, 2016 |
| | NIS in millions | | |
| Total business revenues (consolidated) | 2,064 | 1,868 | 1,745 |
| Profit from revaluations (consolidated) | 218 | 500 | 711 |
| Business profits (consolidated)** | 1,741 | 1,885 | 2,012 |
| Same property NOI (consolidated) | 1,336 | 1,327 | - |
| Same property NOI (corporation's share) | 1,331 | 1,323 | - |
| Total NOI (consolidated)** | 1,523 | 1,385 | 1,301 |
| Total NOI (corporation's share)** | 1,518 | 1,381 | 1,296 |

* For details with respect to additional financial indicators which were examined by the Company, see Sections 2.7 to 2.8 of the Board of Directors' Report.

** The figures include the NOI of Palace Modi'in and Palace Tel Aviv Medical and Palace Ra'anana LTC Units according to the management's position, which deems them part of the NOI of the senior homes although they are not investment properties (and therefore, the tables of the property chapter below shall not include information in respect thereof) and due to non-materiality in their separate presentation.

### 7.2.2 Summary of the results in the retail centers and malls in Israel segment

| | For the year ended on | | |
|---|---|---|---|
| | Dec. 31, 2018 | Dec. 31, 2017 | Dec. 31, 2016 |
| | NIS in millions | | |
| Total business revenues (consolidated) | 1,034 | 1,032 | 974 |
| Profit (loss) from revaluations (consolidated) | (4) | (25) | 220 |
| Business profits (consolidated) | 816 | 803 | 999 |
| Same property NOI (consolidated) | 780 | 789 | - |
| Same property NOI (corporation's share) | 780 | 789 | - |
| Total NOI (consolidated) | 820 | 828 | 779 |
| Total NOI (corporation's share) | 820 | 828 | 779 |

### 7.2.3 Summary of the results in the office and other space for lease in Israel segment

| | For the year ended on | | |
|---|---|---|---|
| | Dec. 31, 2018 | Dec. 31, 2017 | Dec. 31, 2016 |
| | NIS in millions | | |
| Total business revenues (consolidated) | 633 | 489 | 447 |
| Profit from revaluations (consolidated) | 167 | 630 | 517 |
| Business profits (consolidated) | 684 | 1,027 | 886 |
| Same property NOI (consolidated) | 379 | 378 | - |
| Same property NOI (corporation's share) | 379 | 378 | - |
| Total NOI (consolidated) | 517 | 397 | 369 |
| Total NOI (corporation's share) | 517 | 397 | 369 |

### 7.2.4 Summary of the results in the income-producing property in the U.S. segment

| | For the year ended on | | |
|---|---|---|---|
| | Dec. 31, 2018 | Dec. 31, 2017 | Dec. 31, 2016 |
| | NIS in millions | | |
| Total business revenues (consolidated) | 267 | 221 | 229 |
| Profit (loss) from revaluations (consolidated) | (48) | (186) | (82) |
| Business profits (consolidated) | 101 | (65) | 42 |
| Same property NOI (consolidated) | 138 | 121 | - |
| Same property NOI (corporation's share) | 133 | 117 | - |
| Total NOI (consolidated) | 149 | 121 | 124 |
| Total NOI (corporation's share) | 144 | 117 | 119 |

### 7.2.5 Summary of the results in the senior housing segment

| | For the year ended on | | |
|---|---|---|---|
| | Dec. 31, 2018 | Dec. 31, 2017 | Dec. 31, 2016 |
| | NIS in millions | | |
| Total business revenues (consolidated) | 130 | 126 | 95 |
| Profit from revaluations (consolidated) | 103 | 81 | 56 |
| Business profits (consolidated) | 140 | 120 | 85 |
| Same property NOI (consolidated) | 39 | 39 | - |
| Same property NOI (corporation's share) | 39 | 39 | - |
| Total NOI (consolidated) | 37 | 39 | 29 |
| Total NOI (corporation's share) | 37 | 39 | 29 |

## 7.3 The geographic territories in which the Company operates in the investment property segments

As of the Report Date, the Company operates in two main geographic territories, Israel and the U.S Most of the Company's business is in Israel, where the Company operates throughout the country, including North, Center, South and other urban areas, without preference to specific areas and without investing special managerial inputs in specific areas. The Company estimates that the State of Israel constitutes one geographical territory in terms of the risks and yields of the income-producing property business. In the U.S. the Company operates, as of the Report Date, mainly in the cities of Houston and Austin in Texas.

For details regarding the macroeconomic parameters affecting the business in Israel and the U.S., see Section 6 of Chapter A herein.

## 7.4 Breakdown of the investment property business

Set forth below are details of the Company's investment property business, in four segments: the malls and retail centers in Israel, the office and other space for lease in Israel, senior homes and the land designated for these segments, and income-producing property in the U.S., on a consolidated basis, broken-down by the various uses of the space of each segment. The commercial use in Israel in the tables below is attributed to the retail centers and malls operating segment, whereas the office, industrial and residential uses are attributed in Israel to the office and other space for lease operating segment (and do not constitute operating segments in and of themselves). Furthermore, as of Q3/2016, the Company's operations in the senior housing segment is being described in the Company's Financial Statements as a separate operating segment, in view of the establishment and expansion of the operations and investment in projects under development in the segment, and therefore the segment is included as a separate column in the following tables. The figures of the income-producing property segment in the U.S. all appear under the U.S. territory, while the amounts with respect to this territory are translated into NIS according to the conversion rate of 1 US Dollar =NIS 3.748.

The following breakdown of uses is in the format in which the information is presented to the Group's management. As a rule, in properties whose main use is commerce, the car park was attached to such use, whereas in properties whose main use is offices, the car park was attached to such use. As for the Tel Aviv Azrieli Center, for the purpose of the Report, the car park space is divided equally between the commercial and office uses, due to its similar contribution to both uses. As for the Herzliya Business Park, as of 2016 for the purpose of the Report, the areas of the car park are divided into 25% for retail and 75% for offices, in view of the increased use of the car park by the visitors of the retail areas. With respect to Rishonim, the areas of the parking lot are divided into

33% for retail and 67% for offices according to the Company's estimation, in connection with the use made thereof.

The following terms shall hereinafter have the meaning set forth beside them:

"Space"/"Area" – the space/area for which rent is paid, with the addition of unleased areas (excluding areas sold or acquired after the Report Date, if any). With respect to senior housing, the area refers to all of the built area of the home, in view of the fact that the rate of the public areas in the senior housing facility that the Company operates, out of the total facility area is relatively large and the public areas are also intended to serve the tenants of the homes.

"Revenues" – all payments made by the tenant, including rent, management fees, profit from electricity, parking fees and other payments, if any.

1. Breakdown of income-producing property space (aggregate) by territories and uses, as of December 31, 2018 (in sqm)

| Territories | Uses | Offices | Industry | Retail | Residence | Senior Housing* | Car Parks | Total | % of total area of properties |
|---|---|---|---|---|---|---|---|---|---|
| Israel | Consolidated | 517,159 | 22,521 | 335,034 | 8,698 | 75,879 | 668,454 | 1,627,745 | 79% |
| | Corporation's share | 517,159 | 22,521 | 335,034 | 8,698 | 75,879 | 668,454 | 1,627,745 | 79% |
| U.S. | Consolidated | 246,393 | - | - | - | - | 195,010 | 441,403 | 21% |
| | Corporation's share | 236,478 | - | - | - | - | 192,232 | 428,710 | 21% |
| Total | Consolidated | 763,552 | 22,521 | 335,034 | 8,698 | 75,879 | 863,464 | 2,069,148 | 100% |
| | Corporation's share | 753,637 | 22,521 | 335,034 | 8,698 | 75,879 | 860,686 | 2,056,455 | 100% |
| % of total property area | Consolidated | 37% | 1% | 16% | - | 4% | 42% | 100% | |
| | Corporation's share | 37% | 1% | 16% | - | 4% | 42% | 100% | |

* 786 residential units – adjoined residential units are treated as one unit.

2. Breakdown of income-producing property space (aggregate) by territories and uses, as of December 31, 2017 (in sqm)

| Territories | Uses | Offices | Industry | Retail | Residence | Senior Housing* | Car Parks | Total | % of total area of properties |
|---|---|---|---|---|---|---|---|---|---|
| Israel | Consolidated | 510,241 | 22,521 | 332,341 | 8,698 | 48,939 | 652,495 | 1,575,235 | 80% |
| | Corporation's share | 510,241 | 22,521 | 332,341 | 8,698 | 48,939 | 652,495 | 1,575,235 | 81% |
| U.S. | Consolidated | 223,137 | - | - | - | - | 167,905 | 391,042 | 20% |
| | Corporation's share | 213,226 | - | - | - | - | 165,127 | 378,353 | 19% |
| Total | Consolidated | 733,378 | 22,521 | 332,341 | 8,698 | 48,939 | 820,400 | 1,966,277 | 100% |
| | Corporation's share | 723,467 | 22,521 | 332,341 | 8,698 | 48,939 | 817,622 | 1,953,588 | 100% |
| % of total property area | Consolidated | 37% | 1% | 17% | - | 3% | 42% | 100% | |
| | Corporation's share | 37% | 1% | 17% | - | 3% | 42% | 100% | |

* 559 residential units – adjoined residential units are treated as one unit.

3. Breakdown of the fair value of income-producing properties (aggregate) by territories and uses, as of December 31, 2018[11]

| Territories | Uses | Offices | Industry | Retail | Residence | Senior Housing* | Total | % of total area of properties |
|---|---|---|---|---|---|---|---|---|
| Israel (NIS in millions) | Consolidated | 8,447 | 100 | 11,833 | 172 | 1,687 | 22,239 | 90% |
| | Corporation's share | 8,447 | 100 | 11,833 | 172 | 1,687 | 22,239 | 90% |
| U.S. (USD in millions) | Consolidated | 687 | - | - | - | - | 687 | 10% |
| | Corporation's share | 665 | - | - | - | - | 665 | 10% |
| Total (NIS in millions) | Consolidated | 11,022 | 100 | 11,833 | 172 | 1,687 | 24,814 | 100% |
| | Corporation's share | 10,939 | 100 | 11,833 | 172 | 1,687 | 24,731 | 100% |
| % of total property value Israel | Consolidated | 44% | - | 48% | 1% | 7% | 100% | |
| | Consolidated | 44% | - | 48% | 1% | 7% | 100% | |

* Gross value, without setoff of the balance of deposits from tenants. The value after setoff of the tenant deposits balance is approx. NIS 809 million.

4. Breakdown of the fair value of income-producing properties (aggregate) by territories and uses, as of December 31, 2017 [12]

| Territories | Uses | Offices | Industry | Retail | Residence | Senior Housing* | Total | % of total area of properties |
|---|---|---|---|---|---|---|---|---|
| Israel (NIS in millions) | Consolidated | 7,832 | 96 | 11,673 | 165 | 1,161 | 20,927 | 91% |
| | Corporation's share | 7,832 | 96 | 11,673 | 165 | 1,161 | 20,927 | 92% |
| U.S. (USD in millions) | Consolidated | 566 | - | - | - | - | 566 | 9% |
| | Corporation's share | 545 | - | - | - | - | 545 | 8% |
| Total (NIS in millions) | Consolidated | 9,794 | 96 | 11,673 | 165 | 1,161 | 22,889 | 100% |
| | Corporation's share | 9,721 | 96 | 11,673 | 165 | 1,161 | 22,816 | 100% |
| % of total property value Israel | Consolidated | 43% | - | 51% | 1% | 5% | 100% | |
| | Consolidated | 43% | - | 51% | 1% | 5% | 100% | |

* Gross value, without setoff of the balance of deposits from tenants. The value after setoff of the tenant deposits balance is approx. NIS 503 million.

[11] The fair value of the Group's income-producing properties in Israel is according to valuations the Group received, which were prepared by a certified land appraiser independent of the Company or of the Group companies as of December 31, 2018. As to the properties overseas, the valuations were prepared by certified land appraisers, who are defined as dependent in view of the directives of the ISA due to the indemnification given to them (excluding a non-material property in the amount of approx. NIS 40 million whose value was updated by the Company).

[12] The fair value of the Group's income-producing properties in Israel is according to valuations the Group received, which were prepared by a certified land appraiser independent of the Company or of the Group companies as of December 31, 2017. As to the properties overseas, the valuations were prepared by certified land appraisers, who are defined as dependent in view of the directives of the ISA due to the indemnification given to them (excluding a non-material property in the amount of approx. NIS 39 million whose value was updated by the Company).

5. Breakdown of NOI of income-producing properties (aggregate) by territories and uses, for the year ended December 31, 2018

| Territories | Uses | Offices | Industry | Retail | Residence | Senior Housing* | Total | % of total property NOI |
|---|---|---|---|---|---|---|---|---|
| Israel (NIS in millions) | Consolidated | 506 | 7 | 820 | 4 | 37 | 1,374 | 90% |
| | Corporation's share | 506 | 7 | 820 | 4 | 37 | 1,374 | 91% |
| U.S. (USD in millions) | Consolidated | 40 | - | - | - | - | 40 | 10% |
| | Corporation's share | 38 | - | - | - | - | 38 | 9% |
| Total (NIS in millions) | Consolidated | 655 | 7 | 820 | 4 | 37 | 1,523 | 100% |
| | Corporation's share | 650 | 7 | 820 | 4 | 37 | 1,518 | 100% |
| % of total property NOI | Consolidated | 43% | 1% | 54% | - | 2% | 100% | |
| | Corporation's Share | 43% | 1% | 54% | - | 2% | 100% | |

* The figure includes the NOI of Palace Modi'in and Palace Tel Aviv Medical, and Palace Ra'anana LTC Units, as aforesaid.

6. Breakdown of NOI of income-producing properties (aggregate) by territories and uses, for the year ended December 31, 2017

| Territories | Uses | Offices | Industry | Retail | Residence | Senior Housing* | Total | % of total property NOI |
|---|---|---|---|---|---|---|---|---|
| Israel (NIS in millions) | Consolidated | 387 | 7 | 828 | 3 | 39 | 1,264 | 91% |
| | Corporation's share | 387 | 7 | 828 | 3 | 39 | 1,264 | 92% |
| U.S. (USD in millions) | Consolidated | 35 | - | - | - | - | 35 | 9% |
| | Corporation's share | 34 | - | - | - | - | 34 | 8% |
| Total (NIS in millions) | Consolidated | 508 | 7 | 828 | 3 | 39 | 1,385 | 100% |
| | Corporation's share | 504 | 7 | 828 | 3 | 39 | 1,381 | 100% |
| % of total property NOI | Consolidated | 37% | - | 60% | - | 3% | 100% | |
| | Corporation's Share | 36% | 1% | 60% | - | 3% | 100% | |

*The figure includes the NOI of Palace Tel Aviv Medical and Palace Ra'anana LTC Units, as aforesaid.

7. Breakdown of NOI of income-producing properties (aggregate) by territories and uses, for the year ended December 31, 2016

| Territories | Uses | Offices | Industry | Retail | Residence | Senior Housing* | Total | % of total property NOI |
|---|---|---|---|---|---|---|---|---|
| Israel (NIS in millions) | Consolidated | 359 | 7 | 779 | 3 | 29 | 1,177 | 90% |
| | Corporation's share | 359 | 7 | 778 | 3 | 29 | 1,176 | 91% |
| U.S.* (USD in millions) | Consolidated | 32 | - | - | - | - | 32 | 10% |
| | Corporation's share | 31 | - | - | - | - | 31 | 9% |
| Total (NIS in millions) | Consolidated | 483 | 7 | 779 | 3 | 29 | 1,301 | 100% |
| | Corporation's share | 478 | 7 | 778 | 3 | 29 | 1,295 | 100% |
| % of total property NOI | Consolidated | 37% | 1% | 60% | - | 2% | 100% | |
| | Corporation's Share | 37% | 1% | 60% | - | 2% | 100% | |

*The figure includes the NOI of Palace Tel Aviv Medical and Palace Ra'anana LTC Units, as aforesaid.

8. Breakdown of real estate revaluation profit (loss) (aggregate) by territories and uses, for the year ended December 31, 2018

| Territories | Uses | Offices | Industry | Retail | Residence | Senior Housing | Total | % of Total Revaluation Profit |
|---|---|---|---|---|---|---|---|---|
| Israel (NIS in millions) | Consolidated | 155 | 5 | (4) | 7 | 103 | 266 | 122% |
| | Corporation's share | 155 | 5 | (4) | 7 | 103 | 266 | 121% |
| U.S. (USD in millions) | Consolidated | (13) | - | - | - | - | (13) | (22%) |
| | Corporation's share | (12) | - | - | - | - | (12) | (21%) |
| Total (NIS in millions) | Consolidated | 108 | 5 | (4) | 7 | 103 | 218 | 100% |
| | Corporation's share | 109 | 5 | (4) | 7 | 103 | 220 | 100% |
| % of total revaluation profit | Consolidated | 50% | 2% | (2%) | 3% | 47% | 100% | |
| | Corporation's Share | 50% | 2% | (2%) | 3% | 47% | 100% | |

9. Breakdown of real estate revaluation profit (loss) (aggregate) by territories and uses, for the year ended December 31, 2017

| Territories | Uses | Offices | Industry | Retail | Residence | Senior Housing | Total | % of Total Revaluation Profit |
|---|---|---|---|---|---|---|---|---|
| Israel (NIS in millions) | Consolidated | 604 | 4 | (25) | 22 | 81 | 686 | 138% |
| | Corporation's share | 604 | 4 | (25) | 22 | 81 | 686 | 136% |
| U.S. (USD in millions) | Consolidated | (53) | - | - | - | - | (53) | (38%) |
| | Corporation's share | (51) | - | - | - | - | (51) | (36%) |
| Total (NIS in millions) | Consolidated | 418 | 4 | (25) | 22 | 81 | 500 | 100% |
| | Corporation's share | 428 | 4 | (25) | 22 | 81 | 510 | 100% |
| % of total revaluation profit | Consolidated | 84% | 1% | (5%) | 4% | 16% | 100% | |
| | Corporation's Share | 84% | 1% | (5%) | 4% | 16% | 100% | |

10. Breakdown of real estate revaluation profit (loss) (aggregate) by territories and uses, for the year ended December 31, 2016

| Territories | Uses | Offices | Industry | Retail | Residence | Senior Housing | Total | % of Total Revaluation Profit |
|---|---|---|---|---|---|---|---|---|
| Israel (NIS in millions) | Consolidated | 510 | 3 | 220 | 4 | 56 | 793 | 112% |
| | Corporation's share | 510 | 3 | 220 | 4 | 56 | 793 | 111% |
| U.S. (USD in milions) | Consolidated | (21) | - | - | - | - | (21) | (12%) |
| | Corporation's share | (20) | - | - | - | - | (20) | (11%) |
| Total (NIS in millions) | Consolidated | 428 | 3 | 220 | 4 | 56 | 711 | 100% |
| | Corporation's share | 434 | 3 | 220 | 4 | 56 | 717 | 100% |
| % of total revaluation profit | Consolidated | 60% | - | 31% | 1% | 8% | 100% | |
| | Corporation's Share | 61% | - | 30% | 1% | 8% | 100% | |

11. Specification of actual average monthly rent per sqm by territories and uses

| Uses | Offices | | Industry | | Retail | | Residence | |
|---|---|---|---|---|---|---|---|---|
| For the year ended on | | | | | | | | |
| | December 31, 2018 | December 31, 2017 | December 31, 2018 | December 31, 2017 | December 31, 2018 | December 31, 2017 | December 31, 2018 | December 31, 2017 |
| Israel (in NIS) | 85 | 85 | 28 | 28 | 199 | 200 | 42 | 39 |
| Maximum (*) | 110 | (**) 106 | - | - | 321 | 325 | - | - |
| Minimum (*) | 33 | 35 | - | - | 55 | 68 | - | - |
| U.S. (in USD) | 18 | 18 | - | - | - | - | - | - |

The maximum represents the average rent per sqm in the property for which the rent average is highest, whereas the minimum represents the average rent per sqm in the property for which the rent average is lowest. The average was calculated according to the areas suitable for use only. The table does not include figures with respect to the senior housing, in respect of which the average payment of tenants for a residential unit in 2018 is NIS 11,339 per month (in 2017 NIS 11,328 per month) (including revenues from the forfeiture of deposits and payment of monthly maintenance fees).

* The broad range of rent in all of the uses derives, *inter alia*, from the diversity in the nature of the leased property, in the type of the leased unit in the property even in the same building, and in other parameters that are not expressed in this table.

** The maximum represents the average rent per sqm of Azrieli Center towers, and does not include the rent of the hotel. If the average included the rent of the hotel, the average for 2017 would be approx. NIS 101 per sqm.

12. Specification of average occupancy rates by territories and uses*

| Uses | Offices | | | Industry | | | Retail | | | Senior Housing | | | Residence | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Percentage (%) | | | | | | | | | | | | | | | |
| | As of Dec. 31, 2018 | For Y2018 | For Y2017 | As of Dec. 31, 2018 | For Y2018 | For Y2017 | As of Dec. 31, 2018 | For Y2018 | For Y2017 | As of Dec. 31, 2018 | For Y2018 | For Y2017 | As of Dec. 31, 2018 | For Y2018 | For Y2017 |
| Israel | (1)99% | (1)99% | (3)99% | 100% | 100% | 100% | 98% | 98% | 98% | (2)98% | 2)98% ( | 97% | 100% | 100% | 100% |
| U.S. | 84% | 84% | 85% | -- | -- | -- | -- | -- | -- | -- | -- | -- | -- | -- | -- |

* The average occupancy rate was calculated based on the lease agreements' data for the beginning of the period and for the end of each period.

(1) In 2018 excluding the two Phase B buildings of the Azrieli Holon Center, which were opened at the end of 2015 and at the end of Q1/2016 and into which tenants are moving in. The occupancy rate in the office and other space for lease segment including the above is approx. 98% as of December 31, 2018 and approx. 97% for Y2018.

(2) In 2018 excluding Palace Modi'in which was opened at the end of the year and into which residents are moving in. The occupancy rate in the senior housing segment including Palace Modi'in is approx. 81% as of December 31, 2018 and approx. 76% for Y2018.

(3) In 2017 excluding the two Phase B buildings of the Azrieli Holon Center, which were opened at the end of 2015 and at the end of Q1/2016 and into which tenants are moving in as well as the offices in Rishonim and Sarona which opened in 2017. The occupancy rate of the office and other space for lease segment including the above is approx. 95% as of December 31, 2017 and approx. 94% in 2017.

13. Number of income-producing buildings, by territories and uses*

| Uses | Offices | | Industry | | Retail | | Senior Housing | | Residence | |
|---|---|---|---|---|---|---|---|---|---|---|
| | For the year ended | | | | | | | | | |
| | Dec.31, 2018 | Dec. 31, 2017 | Dec.31, 2018 | Dec. 31, 2017 | Dec.31, 2018 | Dec. 31, 2017 | Dec.31, 2018 | Dec. 31, 2017 | Dec.31, 2018 | Dec. 31, 2017 |
| Israel | 12 | 11 | 1 | 1 | 17 | 17 | 3 | 2 | 1 | 1 |
| U.S. | 8 | 7 | - | - | - | - | - | - | - | - |
| Total income-producing properties | 20 | 18 | 1 | 1 | 17 | 17 | 3 | 2 | 1 | 1 |

* A number of properties have several different uses, and in such cases the properties were classified in the table under each of such uses.

14. Breakdown of actual average yield rates (according to year-end value), by territories and uses*

| Uses | Offices | | Industry | | Retail | | Senior Housing** | | Residence | |
|---|---|---|---|---|---|---|---|---|---|---|
| | For the year ended on (percentages) | | | | | | | | | |
| | Dec. 31, 2018 | Dec. 31, 2017 | Dec. 31, 2018 | Dec. 31, 2017 | Dec. 31, 2018 | Dec. 31, 2017 | Dec. 31, 2018 | Dec. 31, 2017 | Dec. 31, 2018 | Dec. 31, 2017 |
| Israel | 5.98% | 5.94% | 7.14% | 7.40% | 6.93% | 7.09% | 3.6% | 6.28% | 2.12% | 2.15% |
| U.S. | 5.78% | 5.81% | -- | -- | -- | -- | -- | -- | -- | -- |

The rate of the yield is a division of the actual NOI by the value of the property as of end of year. In the event of the acquisition of properties or completion of construction thereof in the course of the year, the index does not reflect the rate of the annual yield from these properties. The rate of the actual yield does not constitute the CAP rate that the Group used for revaluation of its properties.

* The figures do not represent representative yield but rather the division of actual NOI by the value of the properties, and do not take into account other influences, such as properties populated, properties purchased during the period, revenues expected from vacant spaces, expected investments in the property etc.

** For the senior housing segment – calculated according to net value (after deduction of the tenant deposits balance) as of end of period.

## 7.5 Projected revenues due to signed lease contracts (NIS in millions)

| Period of Revenue Recognition | | Revenues from Fixed Components | Number of Ending Contracts | Area Contemplated in the Ending Agreements (sqm in thousands) |
|---|---|---|---|---|
| Y2019 | Q/1 | 477 | 243 | 27 |
| | Q/2 | 473 | 278 | 40 |
| | Q/3 | 459 | 217 | 28 |
| | Q/4 | 451 | 304 | 47 |
| Y20120 | | 1,582 | 1,088 | 220 |
| Y2021 | | 1,214 | 826 | 142 |
| Y2022 | | 918 | 626 | 171 |
| Y2023 forth | | 1,934 | 1,149 | 473 |
| Total | | 7,508 | 4,731 | 1,148 |

The revenues figures in the above table, which include revenues from rent, management fees and parking, were calculated based on the basic amounts determined in the lease agreements, linked to the CPI known on December 31, 2018, and based on the following assumptions: (1) The exercise of the tenants' options to extend the lease periods included in the lease contracts, was not taken into account, since the CODM does not review, on a regular basis, the expected revenue figures under the assumption of the exercise of options granted to the tenants to extend the lease period; (2) Lease contracts, the lease period under which has ended, and new lease contracts have not yet been signed with the tenants, were not taken into account; (3) The possibility of sale of the properties or the purchase of new income-producing property, was not taken into account; (4) Fines due to early termination, if any, were not taken into account; (5) The increments to the rent due to percentages of the sales were not taken into account for calculation of the rent, and (6) No change has occurred in the management fees advance payments per tenant in respect of 2018.

The Company's revenues include variable components due to additional revenue from sales alone. The Company does not prepare estimates for revenues from variable components which are immaterial in relation to the Company's revenues from its income-producing properties, and therefore it does not have the information.

The revenue figures specified in the above table are under the assumption that the options for extension of the lease periods included in the lease contracts will not be exercised, although many of the Company's tenants usually extend the lease agreements upon the expiration thereof, according to the extension options specified in the agreements.

The above figures are based on the Company's assessment considering signed agreements as of the Report Date and constitute forward-looking information, as this term is defined in the Securities Law. Actual results may significantly differ from the above specified estimates and the implications thereof, for various reasons, including early termination of lease contracts or a business crisis of any of the tenants.

## 7.6 Main tenants

In 2018, the Company did not have a tenant, the revenue from whom constituted 10% or more of its total revenues.

In 2018, the revenues from the fashion industry accounted for approx. 17% of the Group's revenues and approx. 46% of the revenues from the Company's retail centers and malls segment. If and when material changes shall occur in costs in this segment and insofar as the effect of the changes continues over time, the Company's profitability may also be affected thereby.

However, most of the lease agreements include a fixed rent, such that the Company's exposure in this respect is limited in the short term.

## 7.7 Properties under construction In Israel(*) (aggregate level) by use

| Uses | Parameters | For the Year Ended | | |
|---|---|---|---|---|
| | | December 31, 2018 | December 31, 2017 | December 31, 2016 |
| Retail (4) | Number of properties under construction at the end of the period | 4 | 3 | 4 |
| | Total space under construction (planned) at the end of the period (sqm in thousands) (1) | 88 | 39 | 49 |
| | Total costs invested in the current period (consolidated) (NIS in millions) | 77 | 37 | 207 |
| | The amount at which the properties are presented in the statements at the end of the period (consolidated) (NIS in millions) | 795 | 504 | 941 |
| | Construction budget in the consecutive period (estimate) (consolidated) (NIS in millions) | 45-55 | 30-40 | 90-130 |
| | Total estimated balance of construction budget for completion of the construction work (consolidated) (estimate as of the end of the period) (NIS in millions) (2) | 390-432(6) | 360-400 | 163-195 |
| | Rate of built-up area in respect of which lease contracts have been signed (%) | 1% | 3% | 29% |
| | Projected annual income from projects to be completed in the consecutive period and in which contracts have been signed for 50% of the area or more (consolidated) (estimate) (NIS in millions) | - | - | Approx. 45 |
| Offices and Others (4) | Number of properties under construction at the end of the period | 4 | 3 | 4 |
| | Total space under construction (planned) at the end of the period (sqm in thousands) (1) | 341 | 176 | 227 |
| | Total costs invested in the current period (consolidated) (NIS in millions) | 214 | 50 | 441 |
| | The amount at which the properties are presented in the statements at the end of the period (consolidated) (NIS in millions) | 901 | 507 | 2,043 |
| | Construction budget in the consecutive period (estimate) (consolidated) (NIS in millions) | 352-362 | 145-185 | 245-285 |
| | Total estimated balance of construction budget for completion of the construction work (consolidated) (estimate as of the end of the period) (NIS in millions) (2) | 1,462-1,641(6) | 1,580-1,720 | 485-575 |
| | Rate of built-up area in respect of which lease contracts have been signed (%) | 18% | 15% | 47% |
| | Projected annual income from projects to be completed in the following period and in which contracts have been signed for 50% of the area or more (consolidated) (estimate) (NIS in millions) (4) | - | - | Approx. 165 |
| Residence (4) | Number of properties under construction at the end of the period | 2 | 2 | 2 |
| | Total space under construction (planned) at the end of the period (sqm in thousands) (1) | 55 | 49 | 48 |
| | Total costs invested in the current period (consolidated) (NIS in millions) | 70 | 29 | 16 |
| | The amount at which the properties are presented in the statements at the end of the period (consolidated) (NIS in millions) | 613 | 545 | 523 |
| | Construction budget in the consecutive period (estimate) (consolidated) (NIS in millions) | 100-110 | 50-100 | 35-75 |
| | Total estimated balance of construction budget for completion of the construction work (consolidated) (estimate as of the end of the period) (NIS in millions) (2) | 485-543 | 560-620 | 490-535 |
| | Rate of built-up area in respect of which lease contracts have been signed (%) | - | - | - |
| | Projected annual income from projects to be completed in the following period and in which contracts have been signed for 50% of the area or more (consolidated) (estimate) (NIS in millions) | - | - | - |

| | | | | |
|---|---|---|---|---|
| Senior Housing | Number of properties under construction at the end of the period | 1 | 2 | 2 |
| | Total space under construction (planned) at the end of the period (sqm in thousands) (5) | 44 | 79 | 79 |
| | Total costs invested in the current period (consolidated) (NIS in millions) | 78 | 120 | 111 |
| | The amount at which the properties are presented in the statements at the end of the period (consolidated) (NIS in millions) | 139 | 331 | 207 |
| | Construction budget in the consecutive period (estimate) (consolidated) (NIS in millions) | 232-237 | 245-255 | 185-225 |
| | Total estimated balance of construction budget for completion of the construction work (consolidated) (estimate as of the end of the period) (NIS in millions) (2) | 37-42 | 190-200 | 275-305 |
| | Rate of built-up area in respect of which contracts have been signed (%) | 19% | 20% | 8% |
| | Projected annual income from projects to be completed in the following period and in which contracts have been signed for 50% of the area or more (consolidated) (estimate) (NIS in millions) (3) | - | - | - |

* The Company has no properties under construction outside of Israel.

(1) Marketable space.

(2) Balance of construction budget after the expiration of the consecutive period.

(3) There are no projects that expected to be completed in the consecutive period in which contracts for 50% or more of the area have been signed.

(4) Projects which combine several uses were split among the various uses.

(5) Scope of building rights.

(6) In one of the projects under construction, referring to excavation, shoring and Stage A parking budget only.

## PROPERTIES UNDER DEVELOPMENT – FURTHER DETAILS:

Set forth below is a specification regarding the main new properties under development as of the Report Date in the operating segments of investment property and in the senior housing segment. For further details see Section 4.1 of the Board of Directors' Report:

### Azrieli Sarona, Tel Aviv

In May 2011, the Company purchased the entire long-term lease rights in a lot of an area of approx. 9.4 thousand sqm in the Sarona complex in Southern Hakirya in Tel Aviv, for the construction of an office and retail project. The construction of the project's office tower was completed in Q2/2017. The construction of the mall at the basis of the office tower is expected to be completed in the course of 2019. A certificate of occupancy for a part of the mall's western façade was received in January 2019. The office tower has been fully marketed.

For further details, see Section 4.1.1 of the Board of Directors' Report.

### Azrieli Town

On October 22, 2012, the Company won a tender for the purchase of the rights of Clalit Health Fund in a lot in the area of approx. 10thousand sqm on 146 Menachem Begin Road in the Northern Tel Aviv Central Business District. Construction commenced in September 2016. The project is expected to include approx. 4,000 sqm of retail space and two towers – an office tower with approx. 50,000 sqm of leasable space and a residential tower with some 210 rental apartments. The Group is working to change the zoning plan to increase the building rights at the site. The project is adjacent to the Azrieli Towers and the retail and office parts of the project are scheduled to be completed in 2020. As of the Report Release Date, the Company has signed agreements for the lease of areas in the scope of approx. 41 thousand sqm, which represent approx. 82% of the leasable office space in the project. In May 2018, an above-ground permit was received for the project. In November 2018, a zoning plan was published for deposit, for the addition of employment and hotel areas in a total scope of approx. 24 thousand sqm (gross).

For further details see the Company's immediate report of September 1, 2016 (Ref.: 2016-01-115657), which is included herein by way of reference and Section 4.1.1 of the Board of Directors' Report.

### Palace Lehavim Senior Housing

In December 2014, the Company won a tender issued by the Israel Land Authority, for the long-term leasehold of land in the southern town of Lehavim, in the area of approx. 28 thousand sqm with built area (main and service) of approx. 44,000 sqm. The Company intends to construct a senior home for the elderly on the land, which home will comprise 350 residential units, an LTC unit with full medical observation, related services such as a swimming pool, sport center and retail space of up to approx. 1,500 sqm. In May 2018, an application for a modification permit for the project was granted, regarding an addition of an LTC unit, and the permit was received in October 2018. For further details see Section 4.1.1 of the Board of Directors' Report.

### Holon HaManor

In February 2015, the Company won a tender held by the Israel Land Authority for the purchase of 4 employment-designated lots in the employment zone of the city of Holon, in a total area of 12.4 thousand sqm, in consideration for approx. NIS 64 million. Two of the aforesaid lots (approx. 6.2 thousand sqm) serve the Company to construct a project designated for retail and offices, with marketable spaces of approx. 28 thousand sqm. In September 2018 above-ground permit was received for the project. The project is expected to be completed in 2020. A contract was signed with Bezeq The Israel Telecommunication Corp. Limited in respect of approx. 70% of the project's leasable areas. For further details, see Section 4.1.1 of the Board of Directors' Report.

### Expansion of the Azrieli Tel Aviv Center (the Spiral Tower)

In May 2013, the Company engaged in an agreement for the purchase of full title to the land of approx. 8,400 sqm in the intersection of the streets Menachem Begin Road and Noah Moses in Tel Aviv, adjacently to the Azrieli Tel Aviv Center, which held the building known as the "Yediot Aharonot House". On March 31, 2016, the transaction has been closed and possession of the lot has been handed over to the Company. In February 2018 the Company completed the demolition of the said building and began excavation and shoring work. In April 2018 the zoning plan with an urban-mixed designation was validated, which allows uses of retail, offices, hotels, residence and senior housing with aboveground building rights of 147,260 sqm (gross), and, in addition, approx. 3,000 sqm of underground main retail space. The Company intends to construct retail space that will serve to expand the existing mall and a multi-story tower (the Spiral Tower), subject to receipt of the required statutory approvals.

For further details see the Company's immediate report of April 3, 2016 (Ref.: 2016-01-023433), which is included herein by way of reference, and Section 4.1.1 of the Board of Directors' Report.

### Property in the Holon Industrial Zone – Holon 3 (formerly Lodzia)

A property consisting of land with a registered area of approx. 57.5 thousand sqm, located in the Holon Industrial Zone, acquisition of which was closed in April 2016 and two additional lots originally purchased in the framework of an ILA tender and constituting part of the Holon Manor land. The seller was entitled to all of the revenues after deduction of the management expenses of the property (NOI) in the 12 months as of the signing date of the agreement, in a sum estimated at approx. NIS 10 million. In the report period, the Company vacated the tenants from the buildings on the land and completed the demolition of these buildings. In June 2018, excavation and shoring works began and in October 2018 a permit was received for the construction of basements and the Company commenced the work for the construction thereof. In the framework of consolidation of parcels, approx. 30 thousand sqm of building rights have been added to the lot (such that the total building rights in the consolidated lot amount to approx. 250 thousand sqm).

For further details, see the Company's immediate reports of March 2, 2016, March 23, 2016 and April 14, 2016 (Ref.: 2016-01-039331, 2016-01-012798 and 2016-01-048550, respectively) which are included herein by way of reference, Note 13B(17) to the Financial Statements, and Section 4.1.1 of the Board of Directors' Report.

## Betterment of existing properties:

During the Report Period, the Company continued to promote the betterment of existing properties, *inter alia*, as follows:

Azrieli Akko Mall – in September 2018, another discussion was held by the local committee, regarding the application to re-approve the permit for the addition of parking and office floors, in which the application was approved and the Company is acting to fulfill the terms and conditions for receipt of the permit.

Azrieli Jerusalem Mall – the zoning plan for the expansion of the mall, senior housing and office spaces was discussed by the Local Planning & Building Committee, which recommended the deposit of the plan with the District Committee. In July 2018, the District Planning & Building Committee in Jerusalem approved the Company's application to deposit a plan for expansion of the areas of the Azrieli Jerusalem Mall by approx. 100 thousand sqm above ground, which include retail, commerce and senior housing areas, as well as a structure to be built for the Municipality of Jerusalem, and the Company is acting to publish the plan for deposit.

Azrieli Givatayim Mall – the Company completed the renovation of the fast-food court in the mall.

Azrieli Tel Aviv – the Company completed the renovation of the fast-food court in the mall, continues to upgrade the office elevators, and is further acting to renovate the public areas of the project.

Herzliya Business Park – in June 2018, the Local Committee approved for deposit a plan for the addition of two office floors and additional retail spaces in the project. The deposit is subject to the approval of the District Committee.

Palace Ra'anana Senior Home – in June 2018, the Local Committee discussed the objections submitted in respect of the plan, and approved the plan for validation, subject to various amendments. In November 2018 the Company notified the Local Committee of the cessation of the promotion of the plan.

Azrieli Rishonim – a zoning plan for additional office spaces at the office tower of the project was recommended for deposit by the Local Committee and has been referred for discussion by the District Committee.

The Company reviews, from time to time, options to promote zoning plans for additional building rights in its projects.

*The Company's estimates in Section 7.7 of Chapter A herein are forward-looking information, as defined in the Securities Law, which is based on subjective estimates of the Company as of the Report Date, and the materialization thereof, in whole or in part, is uncertain, or they may materialize in a significantly different manner, inter alia, due to factors which are beyond its control, including changes in market conditions, the period of time that shall be required for approval of the building plans for performance and the construction input prices.*

## 7.8 Land (aggregate)

The table below presents a summary of figures on the Company’s land reserves:

| Territory | | For the year ended on: | |
|---|---|---|---|
| | | December 31, 2018 | December 31, 2017 |
| Israel | The amount at which the lands are presented in the financial statements at the end of the period (NIS in millions) | 306 | 550 |
| | Total area of the lands at the end of the period (sqm in thousands) | 49.4 | 109.7 |
| U.S. | The amount at which the lands are presented in the financial statements at the end of the period (USD in millions) | 5 | 6 |
| | Total area of the lands at the end of the period (sqm in thousands) | 13.7 | 13.7 |

As of the Report Date, the construction in some of the Company’s land reserves is impossible due to planning and other restrictions.

## LAND RESERVES – FURTHER DETAILS:

Following are details regarding the lands intended for construction as of the Report Date in the operating segments of investment properties and in the senior housing segment. For further details see Section 4.1.1 of the Board of Directors’ Report:

### Land in Petach Tikva

On September 17, 2017, the Group has engaged in an agreement for the purchase of land in Petach Tikva of an area of around 19,000 sqm for NIS 91 million together with lawful VAT. On November 9, 2017, the transaction was closed and the possession of the land was handed-over to the Group. The land is situated in the eastern part of the Kiryat Aryeh Industrial Zone in Petach Tikva, near an existing office project owned by the Group. The land includes building rights for around 53,000 sqm as well as parking basements. As of the Report Release Date, the Company promotes a zoning plan for additional rights, based on a zoning plan which is promoted by the municipality in this area, such that its rights will total approx. 150 thousand sqm. The Group intends to build an office project on the land.

For further details, see the Company's immediate reports of September 18, 2017 and November 9, 2017 (Ref.: 2017-01-093630 and 2017-01-098386, respectively) which are included herein by way of reference.

### Senior Housing "Palace Rishon LeZion"

On March 13, 2016, an indirect subsidiary of the Company has won a tender issued by the Israel Land Authority for the purchase of long-term lease rights in a lot of 3.4 thousand sqm designated for senior housing in HaRakafot Neighborhood in East Rishon LeZion, designated for the building of 250 senior housing units and approx. 3,000 sqm of retail, for approx. NIS 26 million. According to the terms of the tender, the consolidated company paid development costs in the amount of approx. NIS 22 million. In April 2018, the recommendation of the Local Committee to deposit a zoning plan for the addition of above-ground building rights was accepted and forwarded for discussion at the District Committee. In November 2018, the District Committee decided to deposit the plan on conditions, and the Company promotes the publication of the plan for deposit.

For further details, see the Company's immediate report of March 13, 2016 (Ref.: 2016-01-005097) which is included herein by way of reference.

### Sale of Pi Glilot Land

On May 10, 2016, the Company and Granite, including through Sonol, sold third parties all of their holdings of land in Pi Glilot and shares of Pi Glilot (which holds the long-term leasehold on land in the Pi Glilot complex), for a total consideration of approx. NIS 130 million. During the Report Period, the transactions have been consummated and the consideration thereof has been paid in accordance with the provisions of the sale agreements.

### Land in Modi'in (lot 21)

On January 11, 2018, the Group had won a tender held by the ILA for the purchase of a leasehold in a lot located in Modi'in-Maccabim-Re'ut CBD (in proximity to the Azrieli Modi'in Mall), on an area of approx. 5,300 sqm, designated for the construction of 80 residential units, 50 hotel rooms, offices and commerce, in consideration for approx. NIS 101.5 million. The Company is acting to increase the building rights in the lot to approx. 28,000 sqm and for its connection to the existing project. In February 2019 a discussion was held at the Local Committee on the addition of rights and it was resolved that the Committees considers favorably the promotion of the plan.

For further details see the Company's immediate report of January 11, 2018 (Ref.: 2018-01-004960), which is included herein by way of reference.

## 7.9 Purchase and Sale of Properties (aggregate)

| Territory | | Parameters (figures of area in thousands and amounts in millions) | Period (Year ended on) | | |
|---|---|---|---|---|---|
| | | | December 31, 2018 | December 31, 2017 | December 31, 2016 |
| Israel (NIS) | Properties Sold | Number of properties sold in the period | 1[(8)] | -- | -- |
| | | Consideration from realization of properties sold in the period (consolidated) | 40 | -- | -- |
| | | Area of properties sold in the period (consolidated) | 6 | -- | -- |
| | | NOI of properties sold (consolidated) | --[(8)] | -- | -- |
| | | Profit / loss due to realization of the properties (consolidated) | -- | -- | -- |
| | Properties Purchased | Number of properties purchased in the period | 2[(9)] | 1[(2)] | 3[(1)] |
| | | Cost of properties purchased in the period (consolidated) [(3)] | 362 | 91 | 847 |
| | | NOI of properties purchased (consolidated) | 6[(10)] | [(6)] | 19[(4)] |
| | | Area of properties purchased in the period (consolidated) | 11[(11)] | 19 | 85 |
| U.S. (US Dollar) | Properties Sold | Number of properties sold in the period | -- | -- | -- |
| | | Consideration from sale of properties in the period | -- | -- | -- |
| | | Area of properties sold in the period (consolidated) | -- | -- | -- |
| | | NOI of properties sold | -- | -- | -- |
| | | Profit / loss in respect of realization of the properties (consolidated) | -- | -- | -- |
| | Properties Purchased | Number of properties purchased in the period | 1[(9)] | [(7)] | 2[(1)] |
| | | Cost of properties purchased in the period (consolidated) | 100 | [(7))] | 174 |
| | | NOI of properties purchased (consolidated) | 7 | -- | 13[(5)] |
| | | Area of properties purchased in the period (consolidated) | 23 | -- | 24 |

(1) In 2016, the Group acquired the following properties: (a) The land of Lodzia in Holon – for details see Section 7.8 of Chapter A herein; (b) Senior housing land in Rishon LeZion – for details see Section 7.8 of Chapter A herein; (c) The Palace Ra'anana Senior Home (in the framework of the acquisition of the Ahuzat Bayit company) – for details see Section 11.1 of Chapter A herein; (d) An office building in Austin, Texas, U.S. – for details see Section 10.1 of Chapter A herein; (e) Land in Houston, Texas, U.S.
(2) In 2017 the Group purchased the following properties: Land in Petach Tikva. For details see Section 7.8 of Chapter A herein.
(3) The costs include the entire purchase amount even if not yet paid and exclude purchase taxes and transaction closing costs.
(4) The NOI only includes Palace Ra'anana Senior Housing and the Ra'anana retail center. The other acquired properties were land.
(5) The NOI only includes the office building in Austin. The additional property is land.
(6) The property purchased is land.
(7) At the end of 2017, the Group increased its holdings in two of its properties located in Houston Texas: 1 Riverway and 3 Riverway.
(8) The sold property is land.
(9) In 2018 the Group acquired the following properties: (a) Land in Modi'in (lot 21) – for details see Section 7.8 of this Chapter A; (b) Real estate rights on Menachem Begin Road in Tel Aviv – for details see Section 1.3.7 of this Chapter A; (c) An office building in Austin, Texas, U.S.A. – for details see Section 10 of this Chapter A.
(10) The NOI includes the real estate rights on Menachem Begin Road in Tel Aviv only, the additional property is land.
(11) Excluding unused rights of approx. 21,000 sqm in land on Menachem Begin Road in Tel Aviv.

## 7.10 Fair value adjustments of values in the Statement of Financial Position required at the corporation level

| | | As of (Consolidated) (NIS in millions) | |
|---|---|---|---|
| | | December 31, 2018 | December 31, 2017 |
| Presentation in the Description of the Corporation's Business Report | Total Income-Producing Property (as presented in the total column in the income-producing properties fair value by territory and use tables as of December 31, 2018 and December 31, 2017 Number 3+4) | 24,814 | 22,889 |
| | Total Income-Producing Property under Construction (as presented in the "Total"column in Table 7.7) in Israel | 2,448 | 1,887 |
| | Total Land for Investment in Israel (as presented in the "Total" column in Table 7.8) | 306 | 550 |
| | Total Land for Investment in the U.S. (as presented in the "Total column in Table 7.8) | 18 | 21 |
| | Consolidated Total | 27,586 | 25,347 |
| Adjustments | Adjustments to value deriving from receivables items | (144) | (110) |
| | Land presented within a property held for sale | - | (40) |
| | Other adjustments[13] | 10 | 9 |
| | Total adjustments | (134) | (141) |
| | Total, After Adjustments | 27,452 | 25,206 |
| Presentation in the Statement of Financial Position | Investment Property Item in the Statement of Financial Position (Consolidated) | 25,004 | 23,319 |
| | Investment Property under Construction Item in the Statement of Financial Position (Consolidated) | 2,448 | 1,887 |
| | Total | 27,452 | 25,206 |

For an explanation with respect to the changes in the investment property items between 2017 and 2018, see Sections 2.10.2, 2.11.2, 2.12.2 and 2.13.2 of the Board of Direcors' Report.

## 7.11 Adjustments to FFO profits

The Company is not required to perform FFO disclosure since the total revenues of the Company from investment properties are lower than 90% of the Company's total consolidated revenues during the report year and year preceding it. In view thereof, the Company calculates FFO profits for the income-producing property business only with the necessary adjustments. For details and a calculation of the FFO profits for the Company's income-producing properties business, see Section 2.7 of the Board of Directors' Report.

[13] In 2018 and 2017, the adjustments are for immaterial costs for projects in early planning stages.

# 8. The retail centers and malls in Israel segment

## 8.1 General information on the operating segment

### 8.1.1 General

Most of the Group's malls and retail centers are spread out throughout the central cities of Israel and are located close to the main traffic thoroughfares which enable easy access and outdoor or indoor parking. The retail centers and malls are optimally planned according to the needs of the population in the area in which the mall is located, and they offer a wide and varied mix of shops in the fields of fashion, footwear, jewelry, gifts, house-wares, communications, electronics and computers, optical devices, entertainment and food complexes for the wellbeing of the visitors, easy access and a large number of parking spaces. The Company puts an emphasis on tenants' mix in each one of the malls and retail centers owned thereby, which it believes shall constitute a center of public attraction to each one of them, in accordance with the characteristics of the local public, and performs suitable marketing work, upgrades and renovates the systems and appearance of the malls and performs technological adjustments. The Company expands the marketing methods of the malls through use of the digital space where most of the end consumers of the retail centers and malls spend time for other purposes, through personal marketing and attractive promotion campaigns, in a manner capable of providing the end-consumer, *inter alia*, a unique shopping experience, which will commence in the digital domain and end in shopping at the Group's malls. Thus, for example, during 2016, the Company launched the Azrieli Malls app, which compiles unique shopping offers and sales at the Group's malls, the ability to pay for parking at the mall and useful information for visitors. The Group also has the Azrieli Gift Card, which is issued either digitally or as a physical card and is redeemable in a broad range of chain stores at the Group's malls.

The Company routinely focuses on the betterment of the Group's existing properties and acts for optimization in the use of its commercial spaces and creates a suitable and modern mix of tenants while differentiating between the projects in order to maintain the relative advantage versus the Group's existing and future competitors.

Most of the Group's lease contracts in Israel are for periods of three to five years and in most cases include an option for additional lease periods (usually three to five additional years), other than agreements in respect of relatively large leasable space, which are mostly signed for longer lease periods ranging between 8 to 25 years (including extensions and exercised options). Most lease agreements include rent that is composed of fixed rent or of rent derived as a percentage of the tenant's turnover in the leased premises, whichever is higher; however, in most cases, the rent actually paid to the Company is the fixed rent, and the Company's revenues from turnover-dependent rent are in an immaterial amount. The occupancy rate of the Group's properties in this operating segment, as of the Report Date, is approx. 98%.

The Group's retail centers and malls in Israel are managed, with relation to each mall or retail center, by designated management companies established by the Group, which enter with the tenants into management agreements for the purpose of management and maintenance of the public areas, in consideration for management fees.

Most of the management agreements determine that the management fees will be paid based on the cost of the management services, plus overhead expenses. The management services include, *inter alia*, marketing services of the mall and/or the retail center, both to visitors and to potential tenants, security services, cleaning of public areas, gardening, maintenance of elevators and public systems. The management companies collect from the tenants the management fees or the maintenance fees, which are used, *inter alia*, for financing the maintenance of public areas. The management company leases from the Group companies, as the case may be, in each of the malls and retail centers, an area in a small scope located in a non-central area of the mall or retail center, to serve as the offices and storage rooms of the management company, in consideration for fixed rent. In most of the management agreements between the management companies and the tenants, the management companies undertake to maintain and operate the public areas in the malls and retail centers, including cleaning, security, renewal, advertising, insurance, under conditions and to the extent that will be determined by the management companies from time to time.

All of the Group's retail centers and malls include also car parks (aboveground and/or underground) which serve the visitors and the potential tenants, with some of the car parks being open to the general public and some requiring payment.

Above or in proximity to the retail areas in some of the malls and retail centers there are areas designated for lease as offices and other uses such as clinics and gyms. See Section 9 of Chapter A herein for additional details on the office and other space for lease segment.

### 8.1.2 The structure of the operating segment and changes occurring therein

The retail centers and malls in Israel segment is affected by the business activities in the economy, the political and security situation in Israel. Various entities operate in the retail centers and malls segment which locate, plan, construct, lease and maintain properties designated for lease for various uses.

Based, *inter alia*, on publicly-available information, at the outset, most of the malls relied on large anchor tenants, which were considered to be crowd attracting. However, in recent years, the concept has changed for the malls in Israel and an opposite trend has begun, of reduction of the space of the anchors (such as supermarkets and department stores), due to the low rent per sqm paid by such tenants and the large space occupied thereby. However, there are presently “new” anchors in the form of large and leading fashion stores.

Concurrently, the Company is acting to integrate innovative entertainment centers in its malls and retail centers, such as the “Zappa” Club, restaurants and cafés and is acting to bring cinemas back to the malls (thus, agreements have been signed with respect to the building of movie theatres in the Azrieli Haifa mall, Azrieli Hanegev mall and Azrieli Tel Aviv mall), in a way that creates an innovative shopping experience for recreation, leisure and shopping. The Company is also acting to improve its properties by renovating and refreshing the fast- food courts and the public areas.

Note that in recent years, there has been an increase in the retail space intended for the fashion industry in the malls in Israel segment and in the Company's properties in this operating segment. For further details see Section 7.6 of chapter A herein.

In recent years, there has been a noticeable trend of brand fashion retail chains growing strong at the expense of single local stores, including international fashion retail chains, the construction of low-priced power centers outside of cities, which compete with the malls. In addition, an increasingly strengthening trend can be observed in the context of which, several retail groups hold a growing number of leading brands and consequently expand the spaces leased thereby in each mall and necessarily improve their bargaining power vis-à-vis the malls. Furthermore, we are witnessing the development of new formats of large branded family-oriented stores. At the same time, it is noted that from time to time, various chains, including fashion chains, encounter financial difficulties, however, the wide range of businesses and the mix in the Group's malls and retail centers contribute to the reduction of the scope of exposure to events of this kind.

In addition, in recent years, changes have occurred in the Israeli consumer's shopping habits, *inter alia*, in view of the "open skies" reform, which led to a reduction in the prices of flights to various destinations overseas, thereby enabling the execution of more purchases outside Israel as well as online retailing, which brings to the consumer's doorstep a larger variety of products, a quicker and more convenient service and mainly personal tailoring of products according to the consumer’s preferences and habits. The Group is acting to develop ways to combine the new digital retailing and the popular mall experience in a manner which creates a novel consumption experience, through, *inter alia*, Azrieli.com and a designated application.

### 8.1.3 Restrictions, legislation, standards and special constraints applying to the operating segment

This operating segment is subject mainly to the land laws and the land use and zoning laws. In addition, the business in this segment is affected by legislative updates in the field of business licensing, land taxation and municipal taxation. See Section 23 of Chapter A herein for details on the matter of the restrictions, legislation, standards and additional constraints applying to the Group.

### 8.1.4 Changes in the volume of business and profitability of the segment

During recent years, the volume of operations of the Group in the retail centers and malls segment grew, mainly due to the development and construction of new income-producing properties like Azrieli Rishonim Mall that was opened to the public in March 2017 (for a specification of the properties under construction see Section 7.7 of Chapter A herein.) or expansion and renovation of existing properties (construction of the second floor at Azrieli Ayalon, renovation of Azrieli Hanegev mall and Azrieli Jerusalem Mall), as well as the acquisition of existing income-producing properties.

The indicators for activity in 2018 show that the Israeli market is continuing to grow. The gross domestic product, at fixed prices and the gross domestic product *per capita*, increased in 2018 by approx. 3.3% and approx. 1.3% respectively. There was also an increase recorded in the private consumption and private consumption *per capita* by approx. 3.9% and approx. 1.9% respectively. The rate of unemployed is low and in January 2019 is approx. 4.3% and the average compensation in the market increased. Stability was maintained in the income-producing property segment in Israel, both on the demand level and on the rent prices and occupancy rate level. The (known) CPI recorded an 0.1% increase in Q4/2018 and an increase of 1.2% throughout 2018. The Bank of Israel interest rate in 2018 is at the rate of 0.25%. The Prime interest rate is 1.75%.

However, a challenging environment is occasionally felt in negotiations with tenants toward the signing of new lease agreements or the renewal of existing contracts.

During the Report Period an increase was recorded in the average turnover[14] in the Group's malls. In the Company's estimation, coming years may see changes in the competitive balance between the players in the income-producing real estate sector, among other things, in view of the forecast for a decrease in the number of significant new projects which offer retail space, which might strengthen the existing leading malls.

For the Board of Directors' explanations on changes to the fair value of the Group's investment property in this segment as of the Report Date See Section 2.10.2 of the Board of Directors' Report.

The Company's management estimates that the wide dispersion of the portfolio of properties owned thereby, the maintenance and active management of the properties, their location mainly in areas of demand, the high business positioning of the properties and the Company's investment in the betterment of its properties for maintaining such advantage, the high occupancy rates, the broad variety of businesses in the malls and retail centers of the Group and the suitable mix of businesses, and the Company's stable capital structure, contribute to a reduction of the exposure of the Company's businesses to a crisis and/or to significant instability due to the materialization of any of the Company's risk factors.

*The* Company's *aforesaid estimations regarding the changes in the income-producing real estate sector in Israel and the effects of such changes on the Company's results are merely subjective assessments and constitute forward-looking information, within the definition of such term in the Securities Law. Actual results and effects may materially differ from the aforesaid estimations and what they imply for various reasons, including an additional intensification of competition, a decrease in demands and a deterioration in the economic situation in Israel.*

[14] Revenue figures are based on the figures provided by the tenants. In addition, not all of the tenants report to the Group on the revenue figures.

## 8.1.5 Critical success factors in the operating segment and changes occurring therein

The Company estimates that the main success factors in the segment are, *inter alia*: locating retail centers and malls in areas where there is a relatively high level of demand; the right geographic location of retail centers and malls as a response to the needs of the residents in each area; expertise in development, unique architectural planning, management and construction of retail centers and malls through the professional management team; the creation of a mix of diverse, quality tenants with financial strength, know-how and experience in marketing, property management and operation; positive goodwill as well as business positioning and financial strength which allows development at relatively low financing costs and provision of immediate response to attractive business opportunities.

## 8.1.6 Changes to the set-up of suppliers and raw materials for the operating segment

In the framework of the maintenance and management of income-producing properties segment, the Group has no material suppliers with which it engages and it does not purchase raw materials in material scopes.

## 8.1.7 Main barriers to entry and exit of the operating segment and changes occurring therein

Entry Barriers - To the Company's belief, entities operating in the retail centers and malls segment require, primarily, equity and financial strength. The main barrier to entry for the development and construction of a retail center, after finding suitable land in an area of demand, is the need for financial strength that enables to obtain financing for the purpose of the construction, *inter alia*, due to a growing trend whereby developers are increasing investment budgets for lessees of income-producing properties upon the initial lease-up of areas under development. In addition, required mostly are professional knowledge, experience in development segment, positive reputation in the industry, availability of financing sources at good terms and land reserves available and planned in areas with high levels of demand for leasable space for commercial purposes. In addition, entities operating in the retail centers and malls segment are required to meet high regulatory requirements, *inter alia*, zoning, business licensing, safety, accessibility, antitrust and environmental regulation. It is noted, that despite the high barriers to entry, in recent years it was possible to indicate a significant increase in the construction and development of many retail centers, all over Israel. However, the future may bring a decrease in the development and construction of significant projects of malls and large retail centers and a shift towards the development of small, neighborhood centers.

To the Company's belief, the malls' barriers to entry are significantly higher than those of power centers outside the cities, due to the high construction costs that characterize the malls (including the cost of the land, which is more expensive since the locations of the malls are closer to the city centers).

Exit Barriers - exiting this operating segment is mainly contingent on the ability to dispose of properties, which is a direct result of the location of the properties, their physical condition and the condition of the market, as well as various costs, including in connection with land taxation.

## 8.1.8 Structure of competition in the operating segment and changes occurring therein

For a description of the structure of the competition in this operating segment, see Section 8.4 of Chapter A herein.

## 8.1.9 Manner of execution of purchases or construction of properties

The Company's management does not have a fixed policy on the acquisition of properties, and each case is examined on its merits, in view of the business opportunity it presents. The Company examines from time to time business opportunities in Israel and abroad, related to the expansion of its activity, mostly in the real-estate segment, including by way of purchasing land reserves, purchase of additional properties and the improvement of existing properties, as well as the acquisition of activities.

In general, the Company may purchases its rights to properties at times way of direct purchase of the rights to the property, at other times by way of purchasing shares in the companies which own the rights to the properties and at times through an allotment of shares in such companies. As of the Report Date, the Company purchased most of its rights to properties by way of purchasing rights to the properties. The considerations for the purchase or construction of new income-producing properties are based, *inter alia*, on the following parameters: yield from the property; properties which generate steady cash-flows and revenues while prioritizing financially sound tenants; the betterment potential of the purchased property.

The Group's malls and retail centers are either under ownership or under long-term lease from the ILA or long-term lease from the local municipalities in whose territory the property is located.

In transactions in which the registration of rights to the purchased property and its transfer to the name of the Company and or the Group's companies is not finalized by the closing date of the transaction, the Company includes mechanisms in its contracts to secure the fulfilment of the seller' undertakings, including those related to the registration of rights to the property and their transfer to the name of the Company, through the deposit of a part of the consideration in trust and through the lodging of a caveat and/or pledges in favor of the Company, as possible under the circumstances.

Upon the purchase of new properties in respect of which there is an undertaking towards third parties regarding the management and operation thereof, the Company's policy is to release the properties purchased thereby from the management and operation rights, and provide management services itself or through the Group's companies. As of the Report Date, there are no obligations towards third parties in respect of the management and operation of the Group's properties.

The professional managerial team employed by the Group is involved in the construction of all the Group's projects, from the identification of the property, through the preparation of a cost estimate and a timetable for each project, the architectural planning of the project, the carrying-out of contractor bids and up to the ongoing support of the project's construction, with an emphasis on the finish and completion stages thereof and the occupation of each project by the various tenants.

The Company does not consider the disposition of its properties to be a part of its business strategy, however it may act towards the disposition of existing income-producing properties if they are not strategic for the Company and are not in its core business. The Company's management did not set a fixed criterion of required yields in the case of dispositions or purchases and each case is examined on its merits, in view of its circumstances, designation, location and features.

## 8.2 Material properties

Set forth in the table below is a concentration of figures pertaining to material properties of the Group in the retail centers and malls segment as of December 31, 2018 which were evaluated by the valuator Mr. Ronen Katz, a partner at Greenberg Olpiner & co (*) through the income capitalization method:

<table>
<tr><th colspan="3" rowspan="2">Name and features of property</th><th rowspan="2">Year</th><th colspan="11">Information item</th><th>According to Regulation 8b(i) (as applicable)</th></tr>
<tr><th>Fair value/book value at end of period (NIS in millions)</th><th>Revenues from rent during the period (NIS in millions)</th><th>Actual NOI during the period (NIS in millions)</th><th>Rate of Yield (%)</th><th>Adjusted Rate of Yield (%)</th><th>Rate of Yield on the Cost (%)</th><th>Property Value to Debt Ratio (LTV)</th><th>Revaluation profits (losses) (consolidated) (NIS in millions)</th><th>Occupancy rate as of the end of the period (%)</th><th>Average monthly rent per sqm from main use – retail (in NIS)</th><th>Ratio of average revenue per sqm to average rent per sqm**</th><th>Other assumptions underlying the valuation</th></tr>
<tr><td rowspan="6">Azrieli Tel Aviv Mall (1)</td><td>Territory</td><td>Israel</td><td rowspan="2">2018</td><td rowspan="2">2,187</td><td rowspan="2">115</td><td rowspan="2">144</td><td rowspan="2">6.56%</td><td rowspan="2">7.09%</td><td rowspan="2">28%</td><td rowspan="2">0%</td><td rowspan="2">6</td><td rowspan="2">99.5%</td><td rowspan="2">321</td><td rowspan="2">14%[15]</td><td rowspan="2">Main rent cap rate – 7.00[16]. Wighted cap rate – 7.06%.</td></tr>
<tr><td>Functional currency</td><td>NIS</td></tr>
<tr><td>Main use</td><td>Retail</td><td rowspan="2">2017</td><td rowspan="2">2,162</td><td rowspan="2">118</td><td rowspan="2">148</td><td rowspan="2">6.85%</td><td rowspan="2">7.13%</td><td rowspan="2">29%</td><td rowspan="2">0%</td><td rowspan="2">(36)</td><td rowspan="2">100%</td><td rowspan="2">325</td><td rowspan="2">15%[17]</td><td rowspan="2">Main rent cap rate – 7.00%[18]. Wighted cap rate – 7.07%.</td></tr>
<tr><td>Construction cost (NIS in millions)</td><td>512</td></tr>
<tr><td>Corporation's share (%)</td><td>In 2016-2017 – 100%; in 2015 - 99.1%</td><td rowspan="2">2016</td><td rowspan="2">2,181</td><td rowspan="2">118</td><td rowspan="2">147</td><td rowspan="2">6.76%</td><td rowspan="2">7.10%</td><td rowspan="2">29%</td><td rowspan="2">0%</td><td rowspan="2">-</td><td rowspan="2">100%</td><td rowspan="2">329</td><td rowspan="2">14%</td><td rowspan="2">Main rent cap rate – 7.00%[19]. Weighted cap rate – 7.09%.</td></tr>
<tr><td>Area [sqm]</td><td>37,018</td></tr>
</table>

[15] Ratio of average revenue per sqm to average rent and management fees per sqm - 18%.
[16] Approx. 30% of the rent (for large areas) was capitalized according to a cap rate of 6.75%.
[17] Ratio of average revenue per sqm to average rent and management fees per sqm - 18%.
[18] Approx. 29% of the rent (for large areas) was capitalized according to a cap rate of 6.75%.
[19] Approx. 25% of the rent (for large areas) was capitalized according to a cap rate of 6.75%.

| Name and features of property | | | Year | Information item | | | | | | | | | | | According to Regulation 8b(i) (as applicable) |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | Fair value/book value at end of period (NIS in thousands) | Revenues from rent during the period (NIS in thousands) | Actual NOI during the period (NIS in thousands) | Rate of Yield (%) | Adjusted Rate of Yield (%) | Rate of Yield on the Cost (%) | Property Value to Debt Ratio (LTV) | Revaluation profits (losses) (consolidated) (NIS in thousands) | Occupancy rate as of the end of the period (%) | Average monthly rent per sqm from main use – retail (in NIS) | Ratio of average revenue per sqm to average rent per sqm** | Other assumptions underlying the valuation |
| Azrieli Ayalon Mall (2) | Territory | Israel | 2018 | 1,638 | 104 | 115 | 7.05% | 7.23% | 25% | 0% | - | 100% | 259 | 12%[20] | Rent cap rate-7.00%.[21] Weighted cap rate-7.03%. |
| | Functional currency | NIS. | | | | | | | | | | | | | |
| | Main Use | Retail | 2017 | 1,628 | 104 | 115 | 7.08% | 7.25% | 25% | 0% | 3 | 100% | 258[22] | 13[23]% | Rent cap rate-7.00%.[24] Weighted cap rate-7.04% . |
| | Construction cost (NIS in millions) | 512 | | | | | | | | | | | | | |
| | Corporation's share (%) | In 2016-2018 100% | 2016 | 1,610 | 103 | 113 | 7.05% | 7.23% | 25% | 0% | 24 | 100% | 261 | 13% | Main rent cap rate-7.00%[25] Weighted cap rate-7.05%. |
| | Area [sqm] | 33,372 | | | | | | | | | | | | | |

[20] Ratio of average revenue per sqm to average rent and management fees per sqm 15%.
[21] Approx. 41% of the rent (for large areas) was capitalized according to a cap rate of 6.75%.
[22] Comparative figures were amended following a *Lapsus calami*.
[23] Ratio of average revenue per sqm to average rent and management fees per sqm 15%.
[24] Approx. 41% of the rent (for large areas) was capitalized according to a cap rate of 6.75%.
[25] Approx. 39% of the rent (for large areas) was capitalized according to a cap rate of 6.75%.

| Name and features of property | | | Year | Information item | | | | | | | | | | | According to Regulation 8b(i) (as applicable) |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | Fair value/book value at end of period (NIS in millions) | Revenues from rent during the period (NIS in millions) | Actual NOI during the period (NIS in millions) | Rate of Yield (%) | Adjusted Rate of Yield (%) | Rate of Yield on the Cost (%) | Property Value to Debt Ratio (LTV) | Revaluation profits (losses) (consolidated) (NIS in millions) | Occupancy rate as of the end of the period (%) | Average monthly rent per sqm from main use – retail (in NIS) | Ratio of average revenue per sqm to average rent per sqm** | Other assumptions underlying the valuation |
| Azrieli Jerusalem Mall (excluding the office component) | Territory | Israel | 2018 | 2,094 | 131 | 144 | 6.87% | 6.99% | 32% | 0% | 18 | 100% | 284 | 12%[26] | Rent cap rate-6.75%. Weighted cap rate-6.86% . |
| | Functional Currency | NIS | | | | | | | | | | | | | |
| | Main Use | Retail | 2017 | 2,058 | 129 | 144 | 7.01% | 7.02% | 32% | 0% | 29 | 100% | 283 | 13%[27] | Rent cap rate-6.75%. Weighted cap rate-6.87% . |
| | Construction Cost (NIS in millions) | 447 | | | | | | | | | | | | | |
| | Corporation's share (%) | 100% | 2016 | 1,974 | 125 | 138 | 7.01% | 7.15% | 31% | 0% | 76 | 100% | 278 | 12% | Main rent cap rate-6.80% Weighted cap rate-7.09%. |
| | Area [sqm] | 40,229 | | | | | | | | | | | | | |
| The other Properties (other than material)*** | | | 2018 | 13,441 | 819 | 794 | -- | -- | -- | -- | 64 | -- | -- | -- | -- |
| The other Properties (other than material)*** | | | 2017 | 11,984 | 706 | 752 | -- | -- | -- | -- | 121 | -- | -- | -- | -- |
| The other Properties (other than material)*** | | | 2016 | 10,943 | 731 | 692 | -- | -- | -- | -- | 556 | -- | -- | -- | -- |

* Mr. Ronen Katz is a certified real estate appraiser, with B.A. in Agricultural Economy and Administration from the Agriculture Faculty of the Hebrew University in Jerusalem, and has gained experience as a real estate appraiser since 1997.

** The figure is to the Company's best knowledge. It does not include lease agreements which do not include rent from sales and is given based on information received from the tenants or from other third parties (as the case may be), and therefore the Company cannot verify that this information is indeed true.

***In all of the real estate properties' sectors.

(1) The figures include 50% of the profits of the Azrieli Center parking lot (another 50% were included in the details regarding the Azrieli Center offices, as specified in Section 9.4 of Chapter A herein).

(2) The Company is registered in the Land Registration Bureau as a long-term lessee of Azrieli Ayalon Mall for a 49-year period ending on August 1, 2031, with an option for an additional 49-year period. The Municipality of Ramat Gan owns the adjacent car park, which includes approx. 2,350 parking spaces. The Municipality of Ramat Gan has undertaken (and an easement therefor has been registered) to enable a right of passage for vehicles and pedestrians, as well as an open parking right for the public, including the Mall's visitors, in the parking spaces that were arranged (excluding 250 parking spaces, use of which will discontinue insofar as the Municipality realizes building rights thereon) and so long as the Company continues leasing and operating the Azrieli Ayalon Mall. Due to shortage of parking space and use by the neighboring office buildings of the parking areas around the mall, during 2015 an agreement was executed with the Municipality of Ramat Gan for the regulation of parking by marking it in blue and white while reserving the Company's rights in the car park and granting free parking to the mall's visitors at certain times.

[26] Ratio of average revenue per sqm to average rent and management fees per sqm 14%.

8.3 The table below contains a summary of data about a material income-producing building under construction of the Group, as of December 31, 2018. It shall be emphasized that the uses of this property will be divided between the operating segment of the retail centers and malls in Israel and the operating segment of the office and other space for lease in Israel, according to the different uses in the designation of the building rights in the property:

| Name of the Property | Location of the Property | Date of Land Purchase | Actual Share of the Corporation (%) | Method of Presentation in Consolidated Report | Estimated Construction Completion Date | Designated Areas of the Property (by usage) (sqm) | Total Projected Investment, including Land, Construction and Development (NIS in millions) |
|---|---|---|---|---|---|---|---|
| Expansion of Azrieli Center Tel Aviv | Tel Aviv | May 2013 | 100% | Fair value | 2025 | 150,000 sqm for offices, retail and residential | 2,300-2,500 |

[27] Ratio of average revenue per sqm to average rent and management fees per sqm 15.5%.

| Name and Features of the Property | Reporting Period | Financial Data: Aggregate Cost at Year-End, including Land, Construction Development and Financing (consolidated) (NIS in millions) | Financial Data: Data on Fair Value and Revaluations: Fair Value/Book Value at the end of the Period (consolidated) (NIS in millions) | Financial Data: Data on Fair Value and Revaluations: Revaluation Profits (Losses) in the Period (consolidated) (NIS in millions) | Rate of Completion at Year-End [engineering] (%) | Rate of Property's Areas with respect to which Binding Lease Contracts have been Signed as of Year-End (%) | Data on Valuation and its Underlying Assumptions: Valuator's Name and Experience | Data on Valuation and its Underlying Assumptions: Valuation Model | Data on Valuation and its Underlying Assumptions: Additional Underlying Assumptions of the Valuation |
|---|---|---|---|---|---|---|---|---|---|
| Expansion of Azrieli Center Tel Aviv | 2018 | 482 | 756 | 19 | 3% | - | Mr. Ronen Katz is a certified real estate appraiser, with a B.A. in Agricultural Economy and Administration from Faculty of the Agriculture at the Hebrew University in Jerusalem. Experienced from 1997 as a real estate appraiser. | Presented according to fair value under the Comparative method | N/A |
| | 2017 | 458 | 708 | 88 | 2% | - | Mr. Ronen Katz is a certified real estate appraiser, with a B.A. in Agricultural Economy and Administration from Faculty of the Agriculture at the Hebrew University in Jerusalem. Experienced from 1997 as a real estate appraiser. | Presented according to fair value under the Comparative method | N/A |
| Remaining properties under construction 2018 | | 1,532 | 1,693 | 44 | - | - | - | - | - |
| Remaining properties under construction 2017 | | 1,069 | 1,179 | (29) | - | - | - | - | - |

## 8.4 Competition

Beyond the aforesaid, in the Company's estimation, over recent years, the retail centers and malls in Israel segment has been characterized with high competitiveness, and to the best of the Company's knowledge, there are more than 300 retail centers in Israel. The structure, size and business mix of the retail centers are mostly adjusted to the characteristics of the demand of those leasing areas in the geographical region in which they are located. The competition in this area revolves around several parameters, of which the main ones are: (1) the geographical location of the properties and the level of demand for spaces for lease in such area; (2) the level of revenues in the properties; (3) the rent level and management and maintenance costs; (4) the quality of construction of the leased buildings; (5) the level of auxiliary services and, (6) The Lessor's goodwill.

As of the Report Date, the Company operates in that operating segment principally in the development and construction of retail centers, and focuses on discovering reserves of land in attractive locations and with the potential for high revenues, and therefore the competition vis-à-vis bodies which concentrate primarily on acquisitions of existing retail centers is lower. In retail complexes and centers located in residential areas a competition could also develop with local developers. The market trends over the recent years and the attempt to adjust the characteristics of the retail center accurately to local demands and to the substitutes available to the consumer have blurred the lines distinguishing between the different types of retail centers.

Due to the intensification of the competition in the sector, the addition of retail space in many regions and a trend of increase in on-line commerce, the Company acted in 2018 and will continue to act for the development of the end consumer marketing segment. *Inter alia*, the Company continues activity for branding of the Group's malls through a uniform language of communication in the properties themselves, marketing activities and campaigns on the different types of media, and planning of further marketing, branding and differentiation activities and sales campaigns for all of the Group's malls (hard sale).

To the best of the Company's knowledge, a number of entities operate in Israel which hold significant portions of properties in the retail centers and malls segment, including REIT 1 Ltd., Gazit Globe Ltd., Melisron Ltd., Industrial Buildings Ltd., Amot Investments Ltd., Jerusalem Economy Ltd. and Big Shopping Centers (2004) Ltd. In addition, to the best of the Company's knowledge, in recent years new players are joining the market such as the institutional bodies (either directly or through a managing body which knows the operating segment well) and investment funds, that seek alternative yield for the members and for themselves.

The Company estimates that the geographic location of the retail center and its differentiation directly affect its characteristics and its tenant mix since each center adjust itself to the sizes of the geographic market in which it is located in order to create a center of attraction which is unique therefor and deal with centers existing in the area which created the consumers' purchase habits. For the most part, the tenants will consider the benefit of space in a retail center with a better geographic location, a mix conforming to its business operations versus its cost and with a better reputational image.

Competition for the private consumer is also mainly characterized by the geographic location and against other centers of the power center-type as well as shops on city streets. Most of the retail centers and malls serve the population residing or employed in the geographic area in which the retail center is situated. Nonetheless, the Azrieli Tel Aviv Mall, due to its location, accessibility and proximity to the train station and to major intersections, serves consumers from all across Israel.

In the Company's estimation, the competition vis-à-vis the private consumer is influenced, *inter alia*, by the tenant mix, the types of the shops and their branding, the atmosphere and shopping experience, benefits to consumers, events initiated in the framework of the retail center, access to the retail center and available parking (free or paid). The malls and retail centers are therefore required to renovate, upgrade and adjust the tenant mix therein from time to time.

In the Company's assessment, the volume of its business in the retail centers and malls in Israel segment is large, and it is one of the leading companies in the field in Israel. As of the Report Date, approx. 1,900 tenants operate stores and retail in the Group's retail centers and malls. In the Company's estimation, the factors and methods that help the Group cope with the competition in the segment are as follows:

- Most of the retail centers and malls of the Group are characterized by quality planning and a high-quality tenant mix, which the Company carefully maintains over the years and that contribute to its competitive advantage and offer to the visitors to the retail centers and malls a quality shopping experience;
- The volume of the Company's business in the segment allows the Company to engage with chains and service providers at beneficial terms, thus allowing it to specialize in the management of retail centers and malls in an efficient manner in order to lead to savings in costs and in manpower;
- Most of the Company's tenants are large chains and/or companies with superior financial strength and the lease agreements therewith are for a relatively long period;
- The Company's retail centers and malls are located in high-demand areas, enabling the Company to lease the properties to numerous and diverse types of tenants;
- The expertise of the Group in the planning and construction of retail centers and malls according to the needs of the tenants and visitors in the retail center and/or mall.
- The scope of business and the Company's experience in the segment, allows it to carry out marketing activities also to the end consumers, the mall visitors and to adopt innovation in the retail segment, improving the experience of shopping at the Company's shopping centers, including use of digital media. For details with respect to the Company's e-commerce business, see Section 14.1 of Chapter A herein.

## 8.5 Goals and business strategy for the segment

See Section 26 of Chapter A herein for the Company's goals and the Group's strategy.

# 9. The Office and other space for lease in Israel segment

## 9.1 General information on the operating segment

### 9.1.1 General

In this operating segment, the Group operates, as of the Report Date, in the development, construction, acquisition, lease, management and maintenance in Israel of parks for offices and the high-tech industry, office buildings and industrial buildings, workshops, storage and residences. The parks for offices and office buildings are designated primarily for businesses in the segments of liberal professions, service providers, headquarters of financial entities, hotelkeeping, medical services and high-tech industry, which are characterized by a large number of personnel and a demand for adjacent parking spaces.

Most of the Group’s lease agreements are for periods of about five years on average, with the tenant given an option for additional lease periods of about five years and the rent is at a fixed amount per each square meter of the leased space. A recent trend is the engagement in lease agreements for large spaces, for longer periods of around 10 years.

All of the Group’s office and other space for lease properties in Israel include also car parks (above or underground) which serve the tenants and their customers.

In this operating segment, the Group’s income-producing space that are leased to third parties are mainly divided into two types:

- Parks for businesses and for high- tech industries - The Group specializes in responding to the special needs of the high-tech industries and the construction of purpose-built buildings fitted in advance to the needs of the tenants. The purpose-built construction provides a comprehensive and complete solution to tenants, that includes the guidance of the tenant beginning from the stage of preparing the working plans for purposes of the design requested by the tenants, the planning and construction of the building in full cooperation with the tenant and through responding to all of the tenant's demands as to the interior of the leasehold. The business parks present a quality and clean working environment in a central location, quality infrastructure, green areas and parking spaces.
- Office towers - The Group has office towers that are leased, in most cases, with high occupancy to numerous and diverse tenants for long lease periods.

The office and other space for lease segment of the Group in Israel is managed with relation to each building or group of buildings through the Company or designated management companies owned by the Group, which engage with the tenants in management agreements. Most of the management agreements determine that the management fees will be paid on the basis of the cost of the management services plus overhead expenses. The management companies collect from the tenants the management fees or the maintenance fees, which are used, *inter alia*, for financing the maintenance of public areas, whereas in most of the management agreements between the Company or the management companies and the tenants, the management companies undertake to maintain and operate the public areas, including cleaning, security, renewals and insurance, under terms and in the scopes as shall be determined by the management companies from time to time.

### 9.1.2 The structure of the operating segment and the changes occurring therein

The office and other space for lease segment is mainly affected by the economic activities in Israel and abroad. Various entities are active in this operating segment which locate, plan, construct, lease and maintain properties designated for lease for various uses. There are many companies in Israel in the office and other space for lease segment, including large, veteran and leading companies, which own properties in large volumes, as well as smaller, local developers who operate in specific geographic areas. The business in this segment is generally characterized by the fact that part of the costs of construction or acquisition is financed by independent sources and the remainder is financed by credit from outside sources.

### 9.1.3 Restrictions, legislation, standards and special constraints applying to the operating segment

This operating segment is subject mainly to the land laws and the land use and zoning laws. In addition, the business in this segment is affected by legislative updates in the field of business licensing, land taxation and municipal taxation. See Section 23 of Chapter A herein for details on the matter of the restrictions, legislation, standards and additional constraints applying to the Group.

### 9.1.4 Changes in the volume of business and profitability of the segment

To the best of the Company's knowledge, in 2018, the office segment continued, to demonstrate stability, which was reflected in stability in the demand for office space and in stability in the amount of the rent in many projects. Due to a shortage in supply of available high-quality office space in Tel Aviv, the Report Period was characterized by a moderate rise in rent in leading projects in Tel Aviv.

In addition, the soundness recorded in the hi-tech industry, creates, and in the Company's estimate, will continue to create, in the upcoming years, demand for office space due to the projected continued increase in the number of employees in the information technology, information security and cyber sectors. In view of the aforesaid, there is a noticeable increase in the Company's exposure to the high-tech sector, due to the increase in the lease of offices to companies of this sector.

As of the Report Date, the Group has preserved very high occupancy rates in its income-producing properties in the segment and even increased its total revenues from rent. The Company estimates that its financial strength, the strength of the Company's tenants, some of which constitute the leading firms in the economy (AAA tenants), its high liquidity and standing in the financial market are advantages and strengthen its status in the segment. See Section 2.11.2 of the Board of Directors' Report for details concerning the development of the revenues from this operating segment.

In addition, in recent years, the Company has acted to expand its business in this operating segment, *inter* alia, by development and construction of new projects (in recent years, the Company has built the Azrieli Sarona project in Tel Aviv, the Azrieli Holon Center and the office tower in Azrieli Rishonim Mall). Furthermore, as part of the business strategy the Company is examining attractive investment opportunities and the creation of new growth engines also in tangential segments, and possibilities to create a synergy with the other operating segments thereof.

The Company estimates, in view of the aforesaid and due to the expected increase in the supply of new office buildings in the central region, a moderate decrease in the prices of rent may occur in lower-demand areas (Bnei Brak, Ramat Gan and the suburbs of Tel Aviv). The Company estimates that such decrease is not expected to have a very material effect in the long term on the rent prices of the Company's properties, which are essentially characterized by a high quality level of construction, location and management, the level of demand for which in recent years has continuously increased. In addition, a large part of the increase in the supply of offices in the central region is made up of buildings that are being constructed in the context of purchase groups, or buildings that are intended to be sold to a large number of buyers, that are not expected to materially affect the rent prices in the central region. In the Company's estimation, these may increase the supply of leasable office space with respect to spaces for lease of 200-500 sqm. In addition, in the Company's estimation, the coming years may see changes in the competitive balance between the players in the income-producing real estate sector, *inter alia*, due to the lease-up of office space projects, primarily in the Dan Metropolitan Area, which pose challenges for the sector.

*The Company's aforesaid estimations with regard to the changes in the segment and the effect thereof on the Company's results are merely subjective estimations and forward-looking information as per the definition thereof in the Securities Law. The actual results and effects may significantly differ from the estimations specified above and the implications thereof, for various reasons, inter alia, a further strengthening of the competition, a decrease in the demand for office spaces and a worsening of the economic situation in Israel.*

### 9.1.5 Critical success factors in the operating segment and changes occurring therein

The Company estimates that the main success factors of the Company in the segment are, *inter alia*: the geographic dispersion and the location of the income-producing properties in areas in demand throughout Israel for offices, commerce and industry; the quality of the properties; expertise in development and architectural planning; management and construction of properties conforming to potential tenants, in relation to which the Company had engaged in advance in lease contracts through the professional management team employed by the Group; the level of demand and supply of properties of a similar type which dictate the terms of the lease contracts and the potential changes thereto; know-how and experience in marketing, property management and operation; positive goodwill; and business positioning and financial strength which allows immediate response to attractive business opportunities.

### 9.1.6 Changes to the set-up of suppliers and raw materials for the operating segment

Within the framework of this segment, the Group has no material suppliers with which it engages and does not purchase raw materials in material scopes.

### 9.1.7 Main barriers to entry and exit of the operating segment and the changes occurring therein

Barriers to Entry - To the Company's belief, entities operating in this operating segment require mainly equity and financial strength. In addition, professional know-how, experience in the development segment, positive reputation in the industry and available and planned land reserves in areas with high demand for office buildings space for lease bear great importance. Development in the segment requires financial soundness which enables operating in the development segment at relatively low financing costs

Barriers to Exit - exiting this operating segment is conditional, mostly, on the ability to realize properties, which is a direct result of the location of the properties, their physical condition and the condition of the economy, as well as various costs, including in connection with land taxation.

### 9.1.8 Structure of competition in the operating segment and changes occurring therein

See Section 1.1 of Chapter A herein for a description of the structure of competition in this operating segment.

### 9.1.9 Manner of executing acquisitions of the Company

See Section 8.1.9 of Chapter A herein for a description of the manner of acquisition and disposal of the Group's rights in properties.

## 9.2 Competition

The income-producing property segment in general and the office and other space for lease segment in particular, is characterized by a high level of competition. The competition in the office and other space for lease segment in Israel is characterized by a high level of competition which revolves around a number of parameters, the main ones of which are: (1) the geographic location of the properties and the level of demand for spaces for lease in that area; (2) the rent level and management and maintenance costs; (3) the quality of construction of the leased buildings; (4) The level of auxiliary services, and (5) the Lessor's goodwill. The competition in this sector exists both at the stage of identification of the properties for purposes of initiation, development and construction of properties, and at the stage of the leasing of the properties. The Group is exposed in Israel to competition by numerous companies engaging in the lease of business property, in areas of demands similar to those in which the Group's properties are located, while in most cases, the competition is local competition. Thus, for example, the competition for the Azrieli Center is the high priced office buildings in Tel Aviv and the competition for the Herzliya Business Park is other alternate office buildings in that area.

To the best of the Company's knowledge, several bodies are active in Israel, holding significant shares of the office and other space for lease, including REIT 1 Ltd., Gav Yam Land Ltd., Nitzba Holdings 1995 Ltd., Industrial Buildings Ltd., Levinstein Properties Ltd. and Amot Investments Ltd. In the Company's estimation, the scope of its business in the office and other space for lease in Israel segment is among the leading companies in the segment, particularly following the completion of the projects which are under various construction stages, as of the Report Date.

The factors assisting the Company to deal with the competition in this segment are as follows:

- The Company's volume of operation in the segment enables the Company to communicate with companies and service providers at beneficial terms, and it further enables it to specialize in the management of commercial parks and office buildings in an efficient manner which leads to savings in costs and in manpower.
- Most of the Company's tenants are companies with high financial strength and the lease agreements therewith are for a relatively long period of time.
- The Company's office and other space for lease is located in areas of high demand, enabling the Company to lease the properties to numerous diverse types of tenants.
- The unique characteristics of the Group's properties, such as: a retail center in proximity to the office space for rental, access to public transportation, including the railroad and underground car parks for the convenience of the tenants and their customers.
- Most of the Company’s office space is characterized by its high quality and prestigious nature, which distinguishes the Company's property from those of the competing companies and strengthen its competitive edge.

## 9.3 Goals and business strategy in the segment

See Section 26 of Chapter A herein for details on the Company’s goals and the Group’s strategy.

## 9.4 Material Properties

Set forth in the table below is a summary of figures pertaining to material properties of the Group in the office space for lease segment as of December 31, 2018 which were evaluated by the valuator Mr. Ronen Katz, a partner at Greenberg Olpiner & co (*) through the income capitalization method:

| Name and features of property | | | Year | Information item | | | | | | | | | | | According to Regulation 8b(i) (as applicable) |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | Fair value/book value at end of period (NIS in millions) | Revenues from rent in the period (NIS in millions) | Actual NOI in the period (NIS in millions) | Rate of Yield (%) | Adjusted Rate of Yield (%) | Rate of Yield on the Cost (%) | Property Value to Debt Ratio (LTV) | Revaluation profits (losses) (consolidated) (NIS in millions) | Occupancy rate as of the end of the period (%) | Average monthly rent per sqm from main use – retail (in NIS) | Ratio of average revenue per sqm to average rent per sqm** | Other assumptions underlying the valuation |
| Azrieli Sarona Tel Aviv | Territory | Israel | 2018 | 2,429 | 99 | 117 | 4.8% | 7.4% | 8% | 0% | 138 | 99% | 110 | N/A | Main rent cap rate- 7.0%. Weighted cap rate – 7.13%. |
| | Functional currency | NIS | 2017 (until June 2017, the property was under construction | 2,165 | 16 | 15 | 0.7% | 7.8% | 1% | 0% | 388 | 92% | 106 | N/A | Main rent cap rate- 7.25%. Weighted cap rate – 7.34%. |
| | Main use | Offices | | | | | | | | | | | | | |
| | Construction cost (NIS in millions) | 1,514 | | | | | | | | | | | | | |
| | Corporation's share (%) | 100% | | | | | | | | | | | | | |

| Name and features of property | | | Year | Information item | | | | | | | | | | | According to Regulation 8b(i) (as applicable) |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | Fair value/book value at end of period (NIS in millions) | Revenues from rent in the period (NIS in millions) | Actual NOI in the period (NIS in millions) | Rate of Yield (%) | Adjusted Rate of Yield (%) | Rate of Yield on the Cost (%) | Property Value to Debt Ratio (LTV) | Revaluation profits (losses) (consolidated) (NIS in millions) | Occupancy rate as of the end of the period (%) | Average monthly rent per sqm from main use – retail (in NIS) | Ratio of average revenue per sqm to average rent per sqm** | Other assumptions underlying the valuation |
| Azrieli Towers*** | Territory | Israel | 2018 | 3,025 | 177 | 207 | 6.9% | 7.2% | 16% | 9% | (8) | ~100% | **106 | N/A | Main rent cap rate- 6.75%. Weighted cap rate – 6.95%. |
| | | | 2017 | 3,008 | 179 | 210 | 7.0% | 7.2% | 16% | 12% | 111 | 99% | **106 | N/A | Main rent cap rate- 6.75%. Weighted cap rate – 7.06%. |
| | Functional currency | NIS | 2016 | 2,878 | 177 | 209 | 7.3% | 7.5% | 16% | 15% | 53 | 100% | **104 | N/A | Main rent cap rate- 7.0%. Weighted cap rate – 7.34%. |
| | Main use | Offices | | | | | | | | | | | | | |
| | Construction cost (NIS in millions) | 1,292 | | | | | | | | | | | | | |
| | Corporation's share (%) | 100% | | | | | | | | | | | | | |

* Mr. Ronen Katz is a certified real estate appraiser, with B.A. in Agricultural Economy and Administration from the Agriculture Faculty of the Hebrew University in Jerusalem, and has gained experience as a real estate appraiser since 1997.

** Exclusive of hotel rent. If the average were to include the hotel's rent, the average for 2018 would have been approx. NIS 101 per sqm, for 2017 approx. NIS 101 per sqm and for 2016 approx. NIS 99 per sqm.

*** The figures include 50% of the profits from the Azrieli Center parking lot.

For a summary of figures regarding a material property under construction – the expansion of the Azrieli Center (the Spiral Tower), see Section 8.3 of Chapter A herein.

# 10. The income producing property in the U.S. segment

## 10.1 General

As of the Report Release Date, the Group owns eight (8) office rental properties outside of Israel (seven in the U.S.), of a total leasable area of approx. 246 thousand sqm (the Company's share is approx. 236 thousand sqm), which is leased to approx. 250 tenants. The Company's properties in this operating segment do not amount to material properties or very material properties. For aggregate details regarding all of the Company's income-producing properties in this operating segment (including land reserves in Section 7.8 of Chapter A herein), see Section 7 of Chapter A herein, under the geographic territory of the U.S.

About 50% of the Group's office properties in this operating segment are multi-tenant properties and the other 50% are properties with a small number of tenants. All are Class A properties that also include car parks (aboveground or underground) which are used by the tenants. The properties are located in high demand areas with more office building clusters. Unlike the Company's properties in Israel, in some of the Company's properties in the U.S., the Company holds the property together with one or more local partners. As of the Report Date, the Company is routinely examining the expansion of its activity in additional markets, mainly in North America (in addition to Houston and Austin in Texas), with an emphasis on markets where the population of the metropolitan area exceeds two million residents.

The office buildings in the operating segment are mostly intended for businesses (*inter alia* from the energy industry) and service providers which are characterized by a large number of employees and demand for adjacent parking spaces. Most of the Group's lease contracts in this operating segment are for periods of between three and ten years, while often the tenant is given an option for additional lease periods of approx. five years. The rent is at a fixed amount per square meter (or the U.S. customary unit – sq. ft) of the leased area, while often the lease contract includes a rent increase during the term of the lease.

Unlike the Group's office properties in Israel, the Group's office space in the U.S. is managed by external local management companies which act professionally, with which the Company has engaged in agreements, and which the Group is entitled to terminate by advance notice of 30 days. The management companies collect from the tenants the rent, as well as current expenses, such as security, cleaning, maintenance, municipal taxes, insurance, gardening, maintenance of elevators and public systems. The Company examines, on an ongoing basis, possibilities for both operational and property management streamlining.

## 10.2 The structure of the operating segment and changes occurring therein

Between 2011-2018, the Company expanded its business in the U.S. and made several purchase transactions - the first of three office towers in the "Galleria" area of the city of Houston, Texas, and two additional transactions for the purchase of two office buildings in the "Energy Corridor" and “West Belt” area of Houston, Texas. In the course of 2016 the Company purchased an office building in Austin, Texas and a land block in Houston, which is adjacent to a Company-owned property. At the end of 2017, the Company purchased 33.33% and 25% of Riverway 1 and 3, respectively, properties in which the Company already holds 33.33% and 45%. In the course of 2018, the Company purchased an additional office building in Austin, Texas. Most of the Group’s properties in the U.S. are situated in the Houston metropolitan area, which has more than 6 million inhabitants[28] and where population growth in the last 30 years exceeded the U.S. average. Such growth stemmed, *inter alia*, from a high quality of life, a low unemployment rate, the absence of state income tax and an attractive cost of living.

The Group's income-producing property segment in the U.S. is affected by the economic activity in the U.S. economy, and mainly by the economic business in Houston and its office lease market.

[28] The figures are taken from publications of the real estate consulting company Cushman and Wakefield.

The recovery process in Houston after the economic crisis which began in 2008, was among the quickest throughout the U.S. and good figures continued to be recorded in the local economy, mainly thanks to the strong connection that the local economy has with the energy market which experienced a significant price increase until mid-2014. The summer of 2014 saw the beginning of a global downtrend in energy prices, which affected the local economy in 2015-2016. This downtrend was halted in the course of 2017, and a moderate rise in prices began. In early 2018, energy prices continued the slow recovery trend, which was halted in Q4/2018, when energy prices again declined. Until the end of 2018, prices were characterized by significant volatility. The employment situation in the Houston metropolis continues to be stable, with a low unemployment rate. In September 2018 the unemployment rate in the Houston metropolis was 4.1%, in comparison to 4.8% in the previous year[29].

The effect of the decreases of energy prices on the office real estate market in Houston, was reflected in 2016-2018 in various ways such as: A high rate of vacant office spaces, high competitiveness for engagements with new tenants, which increased the costs of the engagement process with these tenants. Furthermore, energy companies offered large spaces in the sublease market, which resulted in a decline in the number of new lease transactions (compared with 2014-2015), and a decrease in the number of projects planned towards commencement of construction. At the same time, the increased willingness of property owners to grant incentives to new tenants such as a high budget for "improvements to the leased property" and a long "grace period".

In addition to the effect of the petrochemicals, gas and energy sector on Houston's economy, to the best of the Company's knowledge, the local economy is also affected by its large medical center (Houston Texas Medical Center), which is the world's largest medical center, as well as the growth in the activity of Houston's port, in which extensive investments were made in recent years, to adjust it to the cargo ships and tankers that recently began to operate in the area.

In August 2017 Houston was struck by the tropical storm "Harvey", which caused numerous flooding incidents, mostly in residential buildings. Two out of the Companies' properties in Houston suffered water damage during the storm. The Company is expected to complete the repair of the damage in the said properties during Q1/2019. It is noted that these properties are covered by an insurance policy. For details regarding the effects of the Company's deductible in 2017, see Note 13D(1) to the Company's financial statements.

In 2016-2018, the Company purchased two office properties in Austin, Texas. Both properties are buildings whose construction had been completed not long before their purchase. The first purchased property is wholly occupied by a high-tech company. The second property, which was purchased in July 2018, is occupied by approx. 11 tenants, most of whom are related to the high-tech and finance industries. One of the growth engines of the demand for office space in Austin is the numerous high-tech companies whose research and development activities are concentrated in this city.

## 10.3 Restrictions, legislation, standards and special constraints applying to the operating segment

This operating segment is subject mainly to the local planning and building laws and land laws. In addition, the business in this segment is affected by legislation and regulation of authorities in the fields of environmental protection, safety, business licensing, land taxation and municipal taxation. For details in the matter of the tax reform in the U.S. see Note 28(A)(3) to the financial statements. See Section 23 of Chapter A herein for details on the matter of the restrictions, legislation, standards and additional constraints applying to the entire Group.

[29] The figures are taken from publications by the real estate company Cushman and Wakefield.

## 10.4 Changes in the volume of business and profitability of the segment

Similar to 2017, 2018 saw a continued trend of increase in vacant space in the Houston office market. The Increase in vacant space derives mainly from a decrease in demand on the part of energy companies consequently to the decrease in energy prices, as well as from an increase in the office space placed on the sublease market. The total rate of vacant space in the Houston metropolitan area grew from 17.3% to 18.6% in the course of 2018, whereas vacant space rate in Class A office buildings was 16.6% at the end of 2018 (the total rate of vacant spaces for lease, including the sublease market was 22.4% at the end of 2018)[30]. In addition, to the best of the Company's knowledge, in 2018, rent prices and tenant incentive packages remained at a level similar to that of 2017. The cost of incentives to tenants in new transactions is similar to that of 2017, however over time this level is relatively high.

## 10.5 Critical success factors in the operating segment and changes occurring therein

The Company estimates that the main success factors in this operating segment are its know-how, expertise and experience in the location and acquisition of attractive properties that will yield a high return, and the location of local management companies specializing in the local market, for the purpose of management of the properties and marketing of the space therein. The Company estimates that the success factors in the acquisition of such properties in the operating segment are, *inter alia*, location of worthwhile transactions and identification of opportunities in the market with a fast response capability, acquisition of properties in attractive, high demand locations with improvement potential, acquisition of properties of a high building and finishing standard, acquisition of properties with a range of related services that are not available in nearby properties which are competing for new contracts, performance of meticulous due diligence investigations, *inter alia* with respect to the expected expense structure in the property and the profit increase potential, the strength of the tenants in the property and the nature of the collateral, as well as knowledge of the financial markets and the various players therein for the purpose of achieving attractive financing terms.

## 10.6 Main barriers to entry and exit in the operating segment and changes occurring therein

Barriers to Entry - To the Company's belief, entities operating in this operating segment require mainly equity and financial strength which allow the acquisition of existing properties at relatively low financing costs. In addition, professional know-how, experience in the segment of acquisitions and management of income-producing properties, as well as know-how and experience in the credit and financing sector are important. Positive goodwill is another important element, both during tenders for the acquisition of income-producing properties and in order to attract attractive tenants to the properties.

Barriers to Exit - exiting this operating segment is conditional, mostly, on the ability to realize properties, which is a direct result of the location of the properties, their physical condition and the condition of the economy, as well as various costs, including in connection with land taxation.

## 10.7 Structure of competition in the operating segment and changes occurring therein

The income-producing property industry, in the U.S., including in Houston and Austin, is characterized by a high level of competition. Competition in this segment revolves around a number of parameters, of which the principal ones are; (1) the geographic location of the properties and the level of demand for the space for lease in that area; (2) the amount of the rent and the management and maintenance costs; (3) the granting of incentives to new tenants or upon renewal of the lease agreement, such as improvements in the leased premises or a certain lease period in which the tenant will not be charged any rent; (4) the quality of construction of the leased buildings; (5)

[30] According to figures appearing in MarketView, Houston, Office Q4 2018, published by CBRE in Q4 2018.

the level of related services; and (6) the reputation of the lessor. The competition in this sector exists both at the stage of acquisition of the properties and at the stage of lease-out of the properties. See Section 10.10 of Chapter A herein for a description of the structure of competition in this operating segment.

## 10.8 Manner of executing acquisitions of the Company

For the purpose of the Group's development in this operating segment, the Group focuses, as of the Report Date, on the acquisition of existing and populated income-producing properties, and is not building new properties itself. In addition, the Company usually enters into financing agreements with different financing bodies for the purpose of the acquisition of the properties in this operating segment, usually under non-recourse terms (with exceptions standard in the U.S. with respect to which a guarantee of the Company is provided). See section 8.1.9 of Chapter A of the Report for a general description of the manner of acquisition and exercise of the entire Group's rights in properties.

## 10.9 Acquisitions performed in the Report Period

On July 12, 2018, the Company, through an (indirectly) wholly-owned American corporation, closed the acquisition of an office building in Austin, Texas, U.S. (the "Property"), in consideration for the sum of approx. U.S. $100.4 million (including transaction costs), from a third party, according to agreements for the purchase of the property. The purchased Property is a 5-floor office building with a total area of approx. 23,214 sqm (approx. 249,870 sq. ft) and an occupancy rate of approx. 100%. The Property also includes approx. 970 parking spaces, most of which are situated in a nearby 7-floor car park. For further details see the Company's immediate report of July 15, 2018 (Ref.: 2018-01-063621), which is incorporated herein by way of reference, and Note 13D(3) to the financial statements.

## 10.10 Competition

The income-producing property segment in the U.S. is, in general, characterized by a high level of competition in all aspects pertaining to the rent, the quality of the finishing of the building and other unique characteristics of the property. The Group is exposed in the U.S. to competition by numerous companies engaging in business property lease, in areas of demands similar to those in which the Group's properties are located. The market of leasable offices in Houston, Texas, constitutes approx. 213.5 million sq. ft of leasable office space (of which approx. 116.4 million sq. ft is defined as Class A), and includes a large number of properties. To the best of the Company's knowledge, several bodies are active in Houston, holding significant shares of the office lease areas segment[31], and the Group's share in the income-producing property segment in the U.S. is negligible.

The factors assisting the Company to deal with the competition in this segment are as follows: (1) The Company's office lease areas are located in high demand attractive areas, enabling the Company to lease the properties to numerous and diverse types of tenants; (2) most of the Group's properties in this operating segment have special characteristics, including: green building rating (LEED certification), financially sound tenants, attractive location adjacent to large retail centers, as well as a high parking space ratio relative to the size of the property; (3) most of the Company's office space in this operating segment is characterized by a high building and finishing standard and has been granted the highest rating level of office properties (Class A).

The Group engages in this operating segment in management agreements with local entities which have vast experience in and deep knowledge of the local market, for the purpose of management and lease of the properties.

## 10.11 Goals and business strategy in the segment

See Section 26 of Chapter A herein for details on the Company's goals and the Group's strategy.

[31] According to figures appearing in MarketView insert, Houston, Office, Q4, 2016 published by CBRE in Q4/2017.

# 11. The Senior Housing Segment

## 11.1. General information about the senior housing segment

The Group's operations in the senior housing segment are presently performed through corporations which are held thereby directly and indirectly, under the "Palace" brand ("Palace" or the "Palace Chain") and it engages in the operation and development of senior homes for the elderly population that feature a high finishing standard and the provision of high-standard related services, which are generally designated for tenants who are capable of leading an independent life. As of the Report Release Date, the Palace Chain employs, directly and indirectly, approx. 560 employees in total. As specified below, all senior homes of the Palace Chain operate long-term care (LTC) units (either inside or adjacently to the senior homes). The construction of LTC units is also planned for senior homes that are under development and construction.

As of the date of this Report, Palace holds and operates three upscale senior homes as specified below:

- Palace Tel Aviv – a senior home in the center of Tel Aviv, including an advanced medical center for recuperation and LTC, also known as "Palace Tel Aviv", which consists of 231 senior home residential units, and "Palace Medical", which contains 136 beds in 4 different units (jointly: "Palace Tel Aviv");
- Palace Ra'anana – a senior home in Ra'anana, including an LTC unit, also known as "Palace Ra'anana" (formerly Ahuzat Bayit), which consists of 324 residential units and 67 LTC beds in two units ("Palace Ra'anana"), as well as an active retail center located adjacently to the senior home and known as Azrieli Ra'anana (formerly: "Park Mall").
- Palace Modi'in – a senior home in Modi'in, which is known as "Palace Modi'in", whose construction ended in the report period, with resident move-ins having commenced in October 2018. Palace Modi'in comprises 239 residential units and approx. 136 LTC beds in 4 different units, of which 34 are recuperation units ("Palace Modi'in"). For further details, see Section 7.7 of this Chapter A.

Palace has also acquired the rights in two sites, on which it is planning and constructing additional senior homes which are in various stages of development and construction, as specified below:

(1) Palace Lehavim – land situated within the Lehavim Local Council, which is in construction stages toward the building of a retirement village, which is expected to include approx. 350 residential units and approx. 72 LTC beds ("Palace Lehavim"); On July 24, 2017, Palace received a permit for the construction of Palace Lehavim. In May 2018, an application for a permit for changes to the project was approved, for the addition of another unit to the LTC wing, and the permit was received in October 2018. For further details, see Section 7.7 of this Chapter A.

(2) Palace Rishon LeZion - in March 2016, the Company won a tender issued by the Israel Land Authority for the purchase of long-term leasehold rights in a lot of approx. 3.4 thousand sqm designated for senior housing and situated in the HaRakafot neighborhood in East Rishon LeZion, which is designated for the construction of approx. 250 residential units, an LTC wing and approx. 3 thousand sqm of retail space ("Palace Rishon LeZion"). The project is at the stages of planning and receipt of approvals. For further details, see Section 7.7 of this Chapter A.

In addition, the Group is promoting a zoning plan for additional rights, *inter alia* for senior housing, in the Azrieli Jerusalem mall.

## 11.2. Structure of the senior housing operating segment and the changes occurring therein

To the best of Palace's knowledge, recent years have seen an increase in the life expectancy of the elderly population in Israel[32], alongside a rise in the standard of living of such population. According to data from the Central Bureau of Statistics (CBS)[33], at the end of 2017, there were approx. 1.02 million residents aged 65 or older living in Israel, representing a rate of approx. 11.6% of the population of Israel's residents. Nearly one half of them (approx. 42%) are older than 75. According to population forecasts, by 2040 persons who are 65 years of age or older will be around 1,900,000 in number, representing approx. 14.3% of the population. According to CBS data and publications by Ma'alot[34], alongside the increase in life expectancy, there is considerable improvement in the standard of living of the elderly, which is reflected in their increased participation in the Israeli employment market, an improvement in their physical, financial and social wellbeing, and an increase in their general satisfaction with their lives. In the elderly housing sector, a distinction may be made between two main solutions: retirement homes and senior homes. Most retirement homes are characterized by elderly residents of middle-to-low socioeconomic status, who are not independent and require constant nursing and medical services. Residents of the traditional retirement homes mostly share one room and their schedule is dictated by the retirement home's operator.

Unlike retirement homes, the senior housing market is aimed at an aged population which is financially established and mostly independent. Senior homes feature modern and luxurious services and facilities, including deluxe complexes that include expansive public areas containing facilities such as: a swimming pool, spa and fitness club, class rooms, restaurant, cafeteria, clinic, and the like. Senior homes provide a respectable and high-quality solution for the elderly, and allow the tenants to lead an independent life in the residential units, along with a social life in the public complexes and the provision of initial medical attention and LTC when necessary. According to estimates of Geocartography, as of the Report Date, the senior housing market consists of approx. 13,000-13,500 senior housing units. As a result of the increase and improvement in the life expectancy of the elderly as described above, and due to the desire of such tenants to conduct an active and social lifestyle, there has been an increase in the demand for senior residential units.

The Senior Housing Law, 5772-2012, which took effect in 2012, and the regulations promulgated thereunder (hereinbelow in this Section, jointly: the "Senior Housing Law"), regulates operations in the Israeli senior housing sector for the first time. The Senior Housing Law prescribes various rules in relation to the permits and requirements for the operation of senior homes, including the duty to receive a senior home operation license, and also prescribes sanctions for the violation of such rules. For additional details with respect to the regulation of the senior housing sector, see Section 23.1.3 of this Chapter A.

### Tenant agreements

Palace's engagements with the tenants of the senior homes are made by means of tenant agreements that grant the tenants the right to use the residential unit and the public areas and also grant them entitlement to the service basket offered and provided by every senior home to its tenants, *inter alia*, in view of the provisions of the Senior Housing Law and by virtue of the relevant engagement agreement. The language of the agreements with the tenants varies among the various senior homes operated by Palace (*inter alia*, considering the fact that some were

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[32] The Central Bureau of Statistics – Press Release of December 11, 2017: "Life expectancy in Israel 2016": https://www.cbs.gov.il/he/mediarelease/DocLib/2017/362/05_17_362b.pdf as well as a release from March 12, 2018 "life expectancy" https://www.cbs.gov.il/he/publications/DocLib/2018/indicators16_1697/prt03_2_h.docx

[33] The Central Bureau of Statistics – Press Release for the International Senior Citizen Day of October 3, 2018: https://www.cbs.gov.il/he/mediarelease/DocLib/2018/284/11_18_284b.pdf.

[34] Ma'alot – The Senior Housing Market in Israel, June 2015 - https://goo.gl/F3oj4I and the Central Bureau of Statistics – Press Release for the International Senior Citizen Day of October 3, 2018: https://www.cbs.gov.il/he/mediarelease/DocLib/2018/284/11_18_284b.pdf.

purchased from previous owners), and according to the time of their signing and the provisions of the law at such time.

As a rule, the engagement is made by means of the standard track, i.e., the deposit forfeiture track, which includes the resident depositing a deposit for the duration of the term of the agreement. In most cases, the amount of the deposit is determined according to the location of the home and the services provided thereby, the size of the apartment and the finishing level, the levels of demand, and more (the "Deposit"). The tenant agreement determines the period over which the deposit will be forfeited (mostly over the course of 12 years) (the "Forfeiture Period") and the rate at which it will be forfeited every year (mostly at a rate ranging between 3% and 4%, plus V.A.T. as required by law). At the elapse of the Forfeiture Period, the forfeiture of the Deposit comes to an end and the balance of the principal plus linkage differentials is repaid to the tenant or his heirs upon the expiration of the tenant agreement and the discontinuance of use of the residential unit.

The tenant agreement also specifies the collateral to be provided to secure the Deposit.

In view of the Group's financial soundness, Palace also enables tenants to engage in alternative tracks to the deposit forfeiture track described above, including a lease track in which the tenant pays rent on a monthly basis etc.; however, the scope of such tracks is significantly smaller than that of the track described above.

In addition to the forfeiture of the Deposit and/or the payment of rent as described above, the tenant agreement provides the amount of the monthly maintenance fees to be collected from the tenant. Subject to the provisions of the Senior Housing Law, Palace may increase the maintenance fees at a real rate and subject to an actual increase in the operating expenses of the home, and, in any event, by no more than the maximum increase rate specified in the tenant agreement.

## 11.3. Restrictions, legislation, standardization and special constraints applicable to the senior housing operating segment

For details with respect to restrictions, legislation, standardization and special constraints applicable to the operating segment, see Section 23.1.3 of this Chapter A.

## 11.4. Changes in the scope and profitability of the senior housing operations

According to the various publications as specified in Section 11.2 of this Chapter A, the increase in life expectancy combined with the increase in population and the improvement in the standard of living among the elderly population targeted by Palace lead to an increase in the scope of demand for high-quality and luxurious senior housing solutions in Israel and to the expansion of Palace's operations in the segment.

Furthermore, the increased awareness of the target group to the advantages of senior housing and the recognition that senior homes for the aged population are a respectable and high-quality solution for this population, while differentiating this operating segment from the image associated with traditional retirement homes, contributes to the development of this segment. As of the Report Date, Palace holds rights in two sites on which it is planning and constructing additional senior homes (Palace Lehavim and Palace Rishon LeZion), and Palace's management expects that their completion and occupancy will increase the scope of its operations in the senior housing segment and turn Palace into a significant and leading agent in the senior housing market in Israel.

*The information regarding the factors which in the estimation of Palace's management may affect the scope of its operations in the senior housing segment and the implications thereof on Palace's positioning as a significant and leading factor in the senior housing market as aforesaid, constitute forward-looking information, as defined in the Securities Law, which is based on the estimations of Palace's management. Such estimations are based on external information sources and subjective assessments by Palace's management. Actual results may differ from the estimations so predicted.*

## 11.5. Developments in the markets or changes in the characteristics of customers

The scope of the operations in the senior housing segment is growing, as a result of the increased life expectancy of the aged population. This trend is also characterized by the desire of parts of such population to preserve the high standard of living and quality of life to which they have become accustomed during the years of their life, and the feeling of loneliness and lack of independence created due to the difficulty in accessibility to the various community services compared with the fulfillment of needs provided by senior housing. In addition, whereas the elderly population had been deterred in the past from moving to senior housing due to the negative image associated therewith and the poor level of services featured thereby, the senior housing setting presently provides a high quality of life while ensuring a safe environment that preserves the tenant's independence, cares for his health, ensures an active daily schedule, which includes culture, sports, social interaction and community, and facilitates living at a high level of comfort in luxurious centers. The entry of leading entities such as Palace into the senior housing sector, which players introduce a modern construction standard of high-level senior homes into the sector, also contributes to the improvement of this image. These developments have brought with them new market demands for expansion of the services offered in senior housing. Therefore, recent years have seen an increased demand for an environment that offers, in addition to the basic services, a variety of social and cultural activities, such as a swimming pool, spa, classes, restaurant, cafeteria, alternative medicine services and more.

## 11.6. Critical success factors in the senior housing operating segment and the changes occurring therein

It is Palace's management's position that there are several critical success factors in the operating segment, which include: (1) Knowledge, experience and management: The senior housing segment is complex and requires experience in and knowledge of issues that are unique to the elderly population, with an emphasis on the operation of senior housing homes. The ability to optimally manage a senior home bears great importance in Palace's coping with the competition against the existing competitors in the sector; (2) Financial soundness: The Group's ability to withstand the costs involved in the construction, purchase and/or operation of premium high-level senior homes is critical to the subsistence of Palace's operations and its positioning as a leading factor in the senior housing market, and may be a central consideration in the choice of a senior home by potential tenants. In addition, Palace's ability to provide collateral to the tenants and repay the funds of the Deposit deposited by them, as mandated by the Senior Housing Law, constitutes, in the estimation of Palace's management, a key success factor; (3) Structure of the senior home, the residential units and the surroundings: Since the senior housing sector is on the course of constant development, both in terms of the quality of the structures and residential units and in terms of the level and variety of services, it is necessary to maintain a high construction and finishing standard in the senior home and the public areas thereof, which constitutes a critical success factor in the sector; (4) Location and nationwide presence: A central and accessible location that also facilitates access to nearby centers, recreation and cultural institutions, convenient access to railway stations and public transportation as well as traffic arteries, in the area of the senior home, constitutes an advantage and a central consideration in the choice of a senior home. Furthermore, the location of the senior home in relation to the place of residence of the children and family and former life center of the tenant is a highly significant factor that affects the tenant's choice of such or other senior home. A more attractive location of the senior home brands it as a more luxurious place and affects the price and the amount of the deposits that may be charged for the residential unit; (5) The size of the residential center: A large residential center consisting of hundreds of residential units entails economies of scale in view of the number and diversity of the tenants residing therein, which enables and creates an abundance of activities and a vibrant community and social life; (6) Reputation and branding: The right branding of a senior home, i.e., the attribution of positive values such as quality, enjoyment, luxury, value for money, the branding of the company running the senior home, years' long reputation, the company's stability, etc., and the creation of a positive position and perception among consumers with respect to the senior home, bear importance in the positioning of the senior home in relation to its competitors; (7) Tenant satisfaction: Tenants who express high satisfaction with their standard of living in the senior home are a major marketing tool vis-à-vis potential clients, which has a high cost-to-benefit ratio. Palace ensures that it is attentive to the needs of the tenants and provides them with a quick response, while maintaining a high level of service and personal response to each and every tenant. Palace also holds various multigenerational events that involve the tenants of the homes and their families in order to expose Palace's senior homes and the services provided thereby to as many potential clients as possible.

## 11.7. Key entry and exit barriers of the senior housing operating segment and the changes occurring therein

In the estimation of Palace's management, the principal barriers for entry into the senior housing operating segment are:

1. The need for unique knowledge, experience and reputation, which are required for the construction and management of a senior home;
2. The need for material capital investments for the purpose of purchase or construction of modern senior housing homes of a high finishing standard and their marketing;
3. The shortage of potentially economically viable land for the construction of senior homes;
4. The ability to comply with regulation requirements that prescribe threshold conditions for the operation of senior homes;
5. The requirement for financial soundness and current cash flow for the purpose of ensuring the ability to repay deposits, and, *inter alia*, the provision of collateral to the tenants according to the provisions of the Senior Housing Law.

In the estimation of Palace's management, the principal barriers for exit from the senior housing operating segment are:

1. The difficulty in finding a purchaser for such operation due to the substantial scope of investment, the knowledge and the experience required for the operation of a senior home under the provisions of the Senior Housing Law;
2. Long-term contractual obligations and the difficulty in evicting tenants within a short time.

## 11.8. Alternatives to the senior housing sector and the changes occurring therein

As of the Report Date, the principal alternative to the senior housing sector is the residence of the elderly in households. In 2017, approx. 97% of persons aged 65 or older were living in households[35]. Among the reasons that may be listed as leading to such high rates, one may specify the improvement in the lifestyle and health of the aged population in recent years, which allow for independent living, and the increase in the variety of services offered to the aged population at home (for example, emergency call centers, medical care at home, etc.). Furthermore, the ability to be assisted by live-in caregivers makes it easier for the elderly to stay at home.

Another alternative to the operating segment is retirement homes which are mostly characterized by elderly residents of middle-to-low socioeconomic status, who are not independent and are in need of constant medical and nursing services, with the cost of residence in such homes being lower than that of senior homes. It is noted

[35] The Central Bureau of Statistics - Press Release for the International Senior Citizen Day of October 3, 2018: https://www.cbs.gov.il/he/mediarelease/DocLib/2018/284/11_18_284b.pdf.

that Palace's management estimates that the existing alternatives on the market do not fully address the social and cultural life aspects that Palace offers in the senior homes, and the sense of security that senior homes provide to their tenants, which constitute a significant consideration when choosing an alternative to senior housing,

## 11.9. Manner of performance of the Group's acquisitions in the senior housing segment

For a description of the manner of purchase and exercise of the Group's rights in properties, see Section 8.1.9 of Chapter A of the Report.

## 11.10. Acquisitions made during and after the Report Period

No acquisitions were made during the Report Period and thereafter.

## 11.11. Competition

To the best of Palace's knowledge, as of the Report Date, there are approx. 50 entities operating approx. 100 senior homes in Israel, among which are Mish'an Center, Mediterranean Towers, Ahuzot Rubinstein, Ad 120, Bayit Bakfar and others, with half of them being located in the center of Israel, primarily in the area of Tel Aviv and Hasharon. In the estimation of Palace's management, the following may be listed among the factors that affect the structure of the competition in the sector: (1) Geographical location, which constitutes a central consideration in the choice of a senior home by potential tenants, who tend to prefer a senior home located in proximity to their family members' place of residence or in proximity to their previous living environment; (2) The nature of the tenants in the senior home and their lifestyle, due to the importance of the cultural and social life that senior homes offer tenants; (3) The standard of the residential units, public areas and other facilities that the senior home offers its tenants; (4) The amount of the deposit and the usage fees collected from the tenants. In Palace's estimation, as of the date of this Report, Palace's market share in the senior housing market is approx. 4.5% based on the presently existing homes and irrespective of the operation of the Medical units.

Principal methods for coping with the competition

In order to preserve Palace's competitive position in the senior housing market and cope with the existing competition, Palace takes, *inter alia*, the following measures:

1. Preserving and ensuring a high standard of services and maintenance in the senior homes. In Palace's estimation, the standard of maintenance and services that Palace provides its tenants is among the highest in the sector.
2. Constructing new senior homes in attractive and competitive geographic locations, built to a high finishing standard that includes public areas, luxurious convenience facilities, including infrastructure for the provision of functional services according to the tenants' needs.
3. Preserving and ensuring a high level of tenant satisfaction, attention to their various needs and quick personal response.
4. Maintenance of an effective marketing and sales layout and branding of the chain as a premium chain under the "Palace" brand.

In the estimation of Palace, its competitive position is favorably affected by the following factors: The reputation and high branding of the existing homes (Palace Tel Aviv, Palace Ra'anana and Palace Modi'in), impeccable management and service, the Group's financial soundness, presence in demanded marketing areas and more.

In the estimation of Palace, its competitive position may be adversely affected by the following factors: entry into and/or expansion of competitors into the senior housing market, mainly in the geographical areas in which Palace operates.

### 11.12. Goals and business strategy in the segment

For a specification of the Company's goals and the Group's strategy, see Section 26 of this Chapter A.

## 12. The Granite Segment

### 12.1. General information about the Granite Segment

The Company, through Canit Hashalom, holds 100% of the issued and paid-up capital of Granite Hacarmel, which is mainly active in the marketing of alternative energy sources (LPG and natural gas) through its subsidiary Supergas, and in the treatment of water, wastewater, air, waste and chemicals for industry, through its subsidiary GES.

### 12.2. Alternative energy sources – general information

In the marketing of alternative energy sources, Granite operates through Supergas.

#### 12.2.1. Marketing of alternative energy sources

Supergas is engaged in the marketing of alternative energy sources such as LPG, natural gas and compressed natural gas ("CNG"). Alternative energy sources are mainly used in the operation of industrial burners, the operation of ovens in bakeries and restaurants, the heating of institutions, the heating of henhouses in agriculture, and in household cooking and heating. In the context of such activity, Supergas purchases locally, imports, stores, markets and distributes LPG to industrial, business, institutional and household customers.

#### 12.2.2. Restrictions, legislation, standardization and special constraints applicable to the operations of Supergas

For details with respect to restrictions, legislation, standardization and special constraints applicable to the operations of Supergas, see Section 12.15 of this Chapter A.

#### 12.2.3. Changes in the scope and profitability of Supergas

See Section 3.1 of the Board of Directors' Report.

#### 12.2.4. Developments in the markets of the Supergas operations or changes in the characteristics of its customers

Recent years have seen an intensification of the competition in the marketing of alternative energy sources in the LPG market, mainly due to an increase in the number of competitors, which leads to a decrease in prices in the sector. However, Supergas' standard of service and reputation are also factors in customers' decisions on the choice of supplier in this sector.

### 12.2.5. Critical success factors in the Supergas operations and the changes occurring therein

The key success factors are: developed marketing, distribution and logistics, reliability of supply, ability to extend credit to customers, a developed billing and collection system, professional knowledge, safety level, service quality and price.

### 12.2.6. Changes in suppliers and raw materials in the operating segment

For details with respect to raw materials and suppliers, see Section 12.13 of this Chapter A.

### 12.2.7. Key entry and exit barriers of the Supergas operations and the changes occurring therein

LPG marketing requires the receipt of a gas supplier license from the Ministry of Energy. The receipt of such license and compliance with the conditions thereof, and with the conditions of additional provisions of the law that apply to those operating in this sector, entail considerable investments in manpower and equipment.

Natural gas operations require engagement for the purchase of natural gas. CNG operations require the receipt of a CNG supplier license from the Ministry of Energy.

Supergas has long-term contractual engagements with suppliers and customers, which might be a barrier to exit the sector. Furthermore, the vacating of various sites and facilities may involve costs and may also serve as an exit barrier.

### 12.2.8. Structure of the competition in the Supergas operations and changes occurring therein

For details with respect to the structure of the competition in the operating segment and changes occurring therein, see Section 12.8 of this Chapter A.

## 12.3. Products and services

Alternative energy sources

Supergas is primarily engaged in the marketing of LPG, natural gas and CNG. Supergas' products serve as energy sources in the operation of industrial burners, the operation of ovens in bakeries and restaurants, the heating of institutions, the heating of henhouses in agriculture, and in household cooking and heating. LPG is marketed to customers in movable gas containers (of 12 kg and 48 kg capacities) and by means of the refilling of gas in immovable bulk gas containers located on the customers' premises. Supergas also markets to its customers LPG-operated devices (water heaters, heaters and household radiators). Natural gas is marketed to customers by means of the natural gas distribution network directly to plants or by means of conveying CNG in containers to plants to which the distribution network has not yet arrived.

## 12.4. Breakdown of revenues and profitability of products and services

Supergas' revenues from the operations of marketing alternative energy sources in 2016 and 2017 and for the Report Period, totaled NIS 505 million, NIS 556 million and NIS 572 million, respectively, which represent approx. 20%-21% of the Company's total revenues on a consolidated basis in each year.

## 12.5. Customers

Supergas' customers in the alternative energy sources segment include industrial customers, various institutional and commercial customers, customers engaged in agriculture, commerce and private households. Supergas is also the only LPG supplier to the Israel Defense Forces (IDF), the Israel Police and the Israel Prison Service.

Supergas' engagements with its commercial customers include installation of the equipment, storage of the LPG, and with some customers – the supply of customer-premises equipment. The term of Supergas' engagement with its customers is affected, *inter alia*, from the amount of investment in the equipment made available to the customer. With its institutional customers, engagements are mostly based on the winning of tenders.

Supergas is not dependent on a single customer or a small number of customers, whose loss would materially affect it. Furthermore, Supergas has no single customer the revenues from whom are 10% or more of the total revenues of Supergas.

## 12.6. Marketing and Distribution

Marketing of alternative energy sources

Supergas markets its products both directly and through independent agents that act to seek and engage with customers. LPG sales to household and small business customers are also carried out through call centers located in the various branches of Supergas. LPG supply to customers is carried out by means of transportation of movable gas containers (of 12 kg and 48 kg capacities) and by means of the transport of LPG in tanks for the purpose of refilling immovable bulk containers (of various capacities) located on the customers' premises.

Supergas, through wholly-owned subsidiaries thereof, markets natural gas and CNG among potential institutional and industrial customers in various regions all across the State of Israel. Supergas specializes in the planning and construction of natural gas and CNG systems, and it provides its customers with services of conversion of the energy systems to working with natural gas. The supply of natural gas to the customers is carried out by means of the gas pipe that runs from the Tamar Reservoir to the natural gas reception terminal at the shores of the State of Israel, and subsequently on to the national transportation system and the regional distribution networks. Supergas is dependent on such gas pipe. In addition, Supergas markets CNG in tanks to plants which the transportation system has not yet reached.

## 12.7. Order backlog

Most of the orders of alternative energy sources' products are delivered a short time before the supply date.

## 12.8. Competition

The alternative energy sources market is characterized by the existence of competition, both with respect to the product types and with respect to the marketing and distribution to commercial, institutional and private customers. The products marketed by Supergas face competition against various fuel products, which are also used in the operation of industrial burners and ovens. In recent years, competition between the companies operating in the segment has increased, which led, *inter alia*, to an increase in discounts to customers, to flexibility in the credit extended to customers and the terms of payment. The market features strong competition, as the product marketed by Supergas and its competitors is uniform.

In LPG marketing, Supergas' main competitors are Pazgas Ltd., the American Israeli Gas Corporation Ltd. (known as Amisragas) and New Dorgas Ltd. There are also several other small gas companies in the market. In the estimation of Supergas' management as of the Report Date, Supergas' market share in LPG marketing is approx. 18%.

In natural gas marketing through the distribution network, Supergas' main competitors are Dor Alon Gas Technologies Ltd., Delek Natural Gas Ltd. and Amisragas. In the marketing of natural gas in its form as CNG, Supergas' main competitor is Delek Natural Gas Ltd.

The principal considerations taken into account by customers when choosing an LPG and natural gas supplier are: a professional engineering and technical layout, supply reliability, safety, service and the price of the product. Supergas dedicates efforts to the improvement of its customer service, *inter alia*, by improving availability, safety and reliability. Supergas further acts to enhance its employees' professional knowledge.

## 12.9. Seasonality

LPG consumption is affected by seasonality. LPG sales in the wintertime are higher, since LPG is used for heating, among other things.

## 12.10. Fixed assets, real properties and facilities

### Alternative energy sources

Supergas operates two main logistic facilities for the storage, refilling and supply of LPG: (1) A storage, refilling and distribution facility in Kiryat Ata in an overall area of approximately 15 thousand sqm. This area is leased by Supergas from the Israel Land Authority. The facility includes LPG warehouses with a permitted storage capacity of approx. 300 tons in bulk tanks and approx. 330 tons in containers; (2) a central logistics center located in the Ramla industrial zone in an overall area of approximately 4.4 thousand sqm. This area is leased by Supergas from the Israel Land Authority. The facility includes a warehouse for the storage of LPG cylinders with a permitted storage capacity of 100 tons, equipment warehouses, a heating department, a workshop, a laboratory and a machining shop; (3) In addition, Supergas leases storage volume of approx. 1,500 tons in the facilities of EAPC in Ashkelon, which allows it, *inter alia*, to import LPG, accumulate a stock of LPG thereby reducing LPG importation in wintertime.

In addition, Supergas also stores LPG in tanks installed on the customers' premises in order to supply it to such customers, and it further lends its customers equipment owned thereby (gas containers, regulators and gas meters) against the deposit of an appropriate deposit according to the Control of Prices of Commodities and services Order (Determination of Supervision Level and Maximum Deposit Prices for Gas Equipment), 5776-2015.

Supergas holds a plant for natural gas compression in the Alon Tavor Industrial Zone, in the total area of approx. 11 thousand sqm. The plan includes an advanced system for the treatment of natural gas that arrives at the plan by means of the transportation network and the compression thereof to high pressure (CNG). CNG is transported to the customers' premises by means of tanker trucks held by Supergas.

## 12.11. Intangible assets

### 12.11.1. Trademarks

Supergas has registered trademarks by which it is recognized as a longstanding, known and dominant company in the Israeli market. The principal trademarks are: "Supergas Israeli Gas Distribution Company Ltd.", which includes Supergas' logo, and "Supergas Natural", which includes the logo of Supergas Natural.

### 12.11.2. Distribution rights

Over the years, Supergas has acquired gas distribution rights from agents that had worked therewith in various geographic areas. The payments paid for the purchase of the rights are presented in the Financial Statements as distribution rights at the reduced cost of NIS 43 million.

### 12.11.3. Licenses

Supergas holds a gas supplier license from the Ministry of Energy for LPG purchase and marketing in portable and immovable containers, GPG storage in portable containers, LPG transportation, LPG refilling in portable containers and LPG bulk storage, LPG purchase and marketing in non-refillable containers and LPG purchase and marketing to gas-operated vehicles in fueling stations. Furthermore, Supergas Home Ltd., a wholly-owned subsidiary of Supergas, holds a gas supplier license for LPG purchase and marketing in portable and immovable containers.

Supergas Natural holds a CNG supplier license from the Gas Authority at the Ministry of Energy for the refilling of CNG tanker trucks via a fixed compression station, and for the transportation of CNG to consumers through CNG tanker trucks.

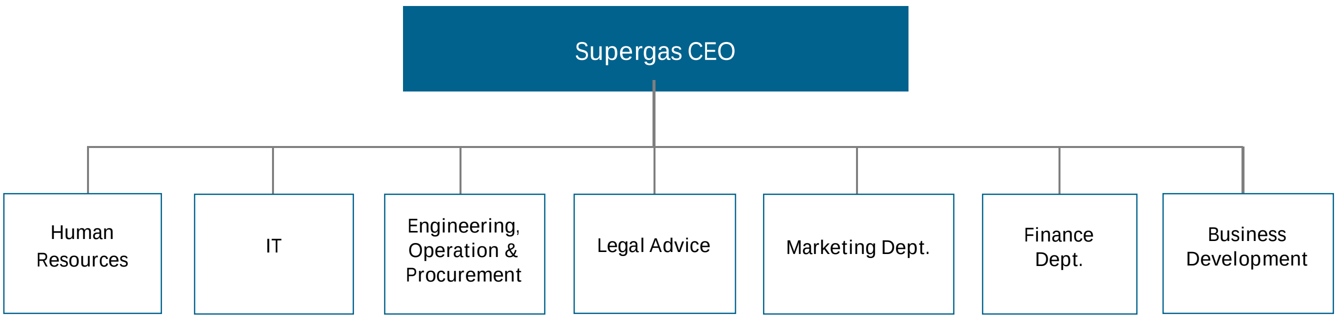
Super N.G. Ltd. ("Super NG") and Super N.G. Hadera and the Valleys Ltd. ("Super NG Hadera") hold licenses for the construction and operation of a natural gas distribution network.

## 12.12. Human capital

### 12.12.1. Organizational structure and workforce

Supergas places a special emphasis on the quality of human capital, by employing professional manpower possessing knowledge and vast experience in the variety of fields required within the areas of its operations. Most of the Company's employees, mainly in the management ranks, have substantial tenure with the Company and extensive experience in the fields of its operations.

### 12.12.2. The following chart describes Supergas' organizational structure as of the Report Date:




As of December 31, 2018, Supergas employs 345 employees. The following table specifies the breakdown of employees into the main fields:

| Position | Number of Employees December 31, 2018 | Number of Employees December 31, 2017 |
|---|---|---|
| Officers and senior management | 6 | 6 |
| Marketing, sales and service | 224 | 239 |
| Finance | 38 | 38 |
| IT | 5 | 4 |
| Human resources and administration | 3 | 2 |
| Engineering, operation and procurement | 69 | 65 |
| Total employees | 345 | 354 |

### 12.12.3. Investments in training, instruction and development of the human capital

Supergas holds professional training and instruction sessions for its employees, according to the employee's position and the needs of Supergas. Supergas' employees participate, *inter alia*, in exhibitions, seminars and study days on various matters pertaining to Supergas. Instruction sessions on safety, fire, work at heights and so forth are conducted according to the duties prescribed by the provisions of the law applicable to Supergas and its operations. Furthermore, a special emphasis is placed on instruction sessions on safety and service.

### 12.12.4. Employment agreements

254 employees employed by Supergas and its subsidiaries are employed under the provisions of two collective bargaining agreements that are periodically updated in negotiations (about every three years).

The collective bargaining agreements regulate the entire employment relations, and, *inter alia*, the employment terms and conditions (including for specific groups such as technicians), social benefits (pension or managers' insurance, advanced study fund, leave, sick leave, recuperation and the like), participation in expenses such as telephone and vehicle, prior notice, dismissal, confidentiality and non-competition, discipline and more.

The employment terms and conditions of other employees, including the officers and senior management employees, are regulated by means of personal agreements and their conditions are individually determined.

## 12.13. Raw materials and suppliers

### Alternative energy sources

Supergas, as other gas companies in Israel, is dependent on Oil Refineries Ltd. ("ORL") and Oil Refineries Ashdod Ltd. ("ORA"), as primary and central suppliers of LPG. In the event that ORL and ORA do not provide Supergas with the quantity of LPG it wishes to purchase therefrom, and Supergas is required to increase the quantity of LPG directly imported thereby, a preparation period will be required and additional costs may be involved. Such import will be subject to and contingent on finding a solution to the existing problem of lack of sufficient storage space for the imported LPG and ability to unload the same. However, it should be noted that ORL and ORA are obligated by law to refrain from discrimination in the supply of LPG to their customers. Due to the increase in LPG consumption in the winter months and the inability of the Israeli refineries to supply such quantities, a shortage of LPG occurs in the winter months. Therefore, Supergas imports LPG. The price of imported LPG is mostly higher than its purchase price from the refineries in Israel.

In 2016, 2017 and 2018, Supergas purchased from Israeli refineries approx. 73%, approx. 68% and approx. 78% of the total amount of LPG purchased thereby, respectively. The rest of the LPG purchased by Supergas was purchased primarily from import.

The State Economy Arrangements Regulations (Legislative Amendments) (Gas Sale by Refineries and Gas Suppliers), 5770-2009, prescribe the quotas to be supplied by refineries to gas marketing companies in months of shortage. See Section 12.15 of this Chapter A with respect to these regulations.

Supergas, as the other natural gas marketers, is dependent on the Tamar reservoir, which is the sole source of natural gas supply to Israel. Supergas has an agreement for the purchase of natural gas with Tamar Partnership, which produces natural gas from the "Tamar" reservoir, and it occasionally purchases natural gas in interruptible transactions from various bodies. In recent years, several other gas reservoirs were found, including the Leviathan Reservoir, and the reservoirs "Karish" and "Tanin" which are a potential gas source for future use. As of the Report Date, commercial use of these reservoirs is yet unavailable.

In Q1/2018, Supergas Natural signed agreements for the purchase of natural gas in the amount of approx. NIS 800 million. The supply period is for approx. 7 years and is expected to commence during 2020. The agreements include mechanisms of a minimal purchase undertaking and compensation as per the standard in similar transactions.

## 12.14. Environmental risks and their management

### 12.14.1. General

Supergas deems environmental protection, the prevention of environmental hazards, and adherence to maximum safety in all components of its business operations, as values of utmost priority. Supergas dedicates great resources and time to realize this purpose. However, due to Supergas' operations and its working with hazardous substances, it involves several environmental risks stemming from the possibility of Supergas' operations leading to various environmental hazards. To cope with such environmental risks, Supergas acts for increased safety in its various operations and for compliance with the mandatory provisions of the law pertaining thereto.

Supergas routinely acts for implementation of and compliance with the provisions of the law and regulation applicable thereto, including the directives and instructions of the Ministry of Energy and the Ministry of Environmental Protection. Supergas is also in constant contact with the municipalities relevant to its operations, the Israel Fire Services and any other relevant authority – all, in order to prevent environmental hazards and minimize potential environmental risks.

### 12.14.2. Environmental risks bearing material implications

LPG is a hazardous substance to both those working therewith and the environment. Improper activity and/or use thereof may cause explosion, flare-up, or poisoning, and consequently harm persons, the environment and property. Working with LPG thus dictates extra care in adhering to various safety rules and taking various precautions, which Supergas follows and acts for assimilation thereof amongst its employees and suppliers. Due to the aforesaid and as shall be further specified below, Supergas' operations is subject to various provisions of law; various regulatory provisions; requires various approvals and licenses and is reviewed by various administrative authorities, such as the Ministry of Energy and the Ministry of Environmental Protection.

Supergas has permits for the construction and operation of LPG repositories across the country, including the logistics center in Ramla and Supergas' refilling, storage and distribution facility in Kiryat Ata. For the past several years, the facility in Kiryat Ata has not had a business license due to the municipality's refusal to grant a business license, as aforesaid. For the legal proceedings conducted by the Company with respect to the gas farm in Kiryat Ata and the conditions required for its operation, see Notes 31B1 and 31B3 to the Financial Statements. Supergas has an approval from the Israel Fire Services for the Kiryat Ata facility, effective until April 2019.

Poison permit – The Hazardous Substances Law, 5753-1993, prescribes that the holding of LPG in a site at which the amount of LPG storage exceeds 8,000 kg requires a “poison permit” from the official in charge authorized by the Minister of Environmental Protection. Furthermore, a poison permit is also required for the natural gas compression plant in Alon Tavor. Following discussions between Supergas and the Ministry of Environmental Protection, the Ministry's approval for the continued operation of the gas farm in Kiryat Ata has been obtained, in the outline specified in the approval issued until June 4, 2019 and permitting Supergas to use the facility subject to conditions specified in the permit. Furthermore, Supergas holds poison permits for the refilling and supply facilities owned thereby.

### 12.14.3. Civil, tortious and criminal liability and administrative sanctions

In view of the nature of its activity and business, Supergas is exposed to various civil, criminal, administrative and tortious claims, inter alia in cases of damage occurring as a result of various incidents related to LPG or natural gas. This may adversely affect Supergas' business results, its business and its goodwill. In order to insure its assets and its liability deriving from the work with hazardous substances as aforesaid, Supergas purchases standard insurance policies which are customary in Israel and which are required by law of Supergas as a licensed gas supplier. Such policies are subject to various exclusions and restrictions. There is no certainty that the coverage and/or the liability caps of the policies cover all of the risks involved in Supergas' business.

In addition, due to the provisions of the law and the regulation applicable thereto, Supergas is exposed to the initiation of criminal proceedings against it, including the filing of indictments against its officers and itself, and to the imposition of various administrative sanctions thereon. A conviction of criminal offenses might lead to a criminal record against the officers of Supergas and against the Company and to the imposition of heavy fines on Supergas. Administrative sanctions against Supergas might lead to the imposition of (temporary or permanent) bans on Supergas' business or parts thereof.

## 12.15. Restrictions and Supervision over the operations of Supergas

The operations of Supergas are subject to laws, regulations and orders which pertain, *inter alia*, to the determination of specific instructions pertaining to the marketing of the products, to the determination of standards of quality, safety, security, storage, labeling and identification of products, transportation, proper business management, consumer protection, environmental protection, price control and various legislation and standardization restrictions. Various regulatory requirements, including ones requiring compliance with strict safety requirements for the purpose of supply of LPG and CNG, compel Supergas to make considerable financial investments in order to comply therewith. Set forth below is a concise review of laws, regulations, orders, restrictions and requirements which are material to Supergas' business:

### Licensing and safety

The Gas Law (Safety and Licensing), 5749-1989 (the "Gas Law") regulates the matter of licensing of gas suppliers and the matter of safety in work with gas. The law requires, *inter alia*, receipt of a license for the supply of gas and for the performance of gas work and receipt of a permit for the installation of gas facilities. The Gas Law further requires that gas systems be tested periodically.

In addition, there are binding standards for gas containers, gas systems, the installation of a central gas system etc. Standardization includes, *inter alia*, a labeling duty, technical instructions, pressure tests and safety tests that must be carried out prior to the supply of gas, as well as the performance of routine periodic tests for LPG containers and for gas systems and facilities.

As gas is defined as a hazardous substance, various activities with gas require permits under the Hazardous Substances Law, 5753-1993 (the "Hazardous Substances Law"). The Hazardous Substances Law prescribes that no person shall work with poisonous substances unless holding a poison permit from the commissioner as defined in the Hazardous Substances Law. Supergas has a general poison permit for its activity and also for facilities thereof which require a poison permit as aforesaid.

In the framework of its operations, Supergas transports, both itself and through subcontractors, LPG and CNG, which, as aforesaid, are deemed hazardous substances. For the purpose of such operation, Supergas holds an appropriate license for transportation and a license for transportation of hazardous substances according to the Transportation Regulations.

## Purchase of LPG from the refineries

In 2007, control over the refineries by way of setting a maximum LPG price was lifted and in its stead, supervision is effected by way of reporting on profitability, prices and quantities. If one or more of the following cases takes place: (1) the refineries fail to comply with the reporting duties applicable thereto in relation to quantities and prices of petroleum products; (2) it transpires that the refinery sold LPG at a price exceeding the import price in the month preceding the month in which the sale was made; or (3) the refinery supplied LPG to different consumers at a different price at the same time - control of the ex-refinery LPG maximum price shall be reinstated.

Furthermore, in 2009, regulations[36] were promulgated, which regulate the matter of LPG sale by the refineries. Among other things, the regulations define new, small and large gas suppliers, and the corresponding gas allocations to such suppliers in months of shortage, i.e. months in which the refinery is unable to supply the full gas demand therefrom.

## Control of LPG prices

The Control of Prices of Commodities and Services Order (Application of the Law to LPG), 5770-2010 prescribes that supervision over LPG will be at the level of reporting on profitability and prices according to Chapter G of the Control of Prices of Commodities and Services Law, 5756-1996 (the “Control of Prices of Commodities and Services Law”). The manner of reporting on LPG profitability was published under the said order in May 2010, and according thereto gas marketing companies, including Supergas, shall annually furnish the Supervisor of Prices with data as stated in the manner of reporting on profitability.

September 2011 saw the publication of the report of the Socioeconomic Change Committee (the “Trajtenberg Committee”), in which report the Trajtenberg Committee proposed to impose, for the short term, control over the ex-refinery and retail LPG prices, which would lead to their reduction. At the same time, the Trajtenberg Committee proposed to set up a governmental team that would propose further reform in the LPG sector.

In May 2013, a letter from the Ministry of Energy was received at Supergas’ offices, from which letter it arises that the Director of the Fuel and Gas Administration and the Supervisor of Prices at the Ministry of Energy are considering recommending the imposition of control over LPG prices in sales via central gas dispensers and via containers to the private sector, further to the supervision at the level of profitability reporting as described above. The letter includes a preliminary draft of attribution of Supergas’ costs to the LPG margin, which was prepared by the Fuel Administration and is based, according to the letter, on data submitted by Supergas and data processing by the Ministry of Energy. Supergas responded to the Ministry of Energy and, *inter alia*, rejected most of the calculations and assumptions underpinning the said letter.

As of the Report Release Date, Supergas is unaware of whether it has been decided to impose such control. It is noted that the State Auditor's report of October 2017 includes a recommendation whereby the Ministries of Energy and Finance should address updated figures regarding the profitability of LPG suppliers in the household sector, while examining the effect of legislation changes that were made in recent years on the competition in this market. Insofar as control is imposed, the manner of its imposition and the implications thereof are unclear. Therefore, Supergas is unable to predict the effect of control on the Company, if and insofar as imposed.

Moreover, the Control of Prices of Commodities and Services Order (Determination of Control Level and Maximum Prices for a Deposit for Gas Equipment), 5776-2015 defines the maximum deposit prices that a gas supplier may

[36] The State Economy Arrangements Regulations (Legislative Amendments) (Gas Sale by Gas Suppliers and Refineries), 5770-2009.

charge a domestic gas consumer for the supply of gas equipment and prohibits the collection of a deposit for gas equipment not listed in the order. The order also sets, *inter alia*, provisions concerning an update of the deposit price and a refund of the deposit to the consumer.

## Promotion of competition in the gas sector

In the context of increasing the competition in gas for domestic consumption, laws and regulations were enacted with respect to the conduct of gas companies vis-à-vis domestic consumers. Such laws and regulations regulate, *inter alia*, the manner of replacing a gas supplier, the prohibition on retention actions vis-à-vis customers who have given a gas supplier replacement notice, the refunding of gas deposits, the grant of option to an incoming gas supplier to purchase the gas tanks from the outgoing gas supplier etc.

Supergas is also subject to various provisions in the framework of its being an entity that provides a service to consumers, both in the context of the Consumer Protection Law (such as scheduling the time for technician arrival, maximum hold time for human telephone response, etc.) and in the context of specific legislation (such as which services are included in the gas price, various provisions concerning the manner of charging for gas consumption, conduct vis-à-vis debtors, etc.).

June 2015 saw the entry into effect of regulations took pertaining to the provision of information concerning gas supply. Such regulations impose a duty on gas suppliers to provide the consumer, on the gas invoice, with the addresses of the other consumers connected to the same central gas system or with an identification code for the supplier's website where such addresses will be available. In addition, gas suppliers are required to transfer, at the beginning of every month, to the Director of the Gas Administration, a report specifying the average prices charged to domestic consumers in the two months preceding the report, broken down by local authority, the type of gas infrastructure (12/48 Kg containers, portable container, immovable container) and the type of service provided (e.g., installation, connection and supply). The Director of the Gas Administration is entitled to post the report also on the website of the Ministry of Energy. Moreover, any gas supplier that has a website is obligated to post the appropriate report on such site.

In addition, additional legislative amendments were made in the Arrangements Law for the Years 2017-2018, the purpose of which is to increase competition in the gas sector and address, *inter alia*, a change of the majority of apartment owners required to replace the gas supplier, the prevention of discrimination between consumers connected to the same tank and in the deposit fees.

The Gas (Safety and Licensing) (Licensing of Gas Suppliers) Regulations, 5779-2018

These regulations replaced the procedure that existed for the granting of a gas supplier license, and accordingly regulate the requirements of any entity wishing to receive a gas supplier license from the Ministry of Energy, including the experience required thereof in the gas sector, the fees that it is required to pay, its obligations as a license holder, insurance requirements, and procedures for submitting the applications to the Ministry of Energy.

The Draft Liquefied Petroleum Gas Bill, 5779-2018 and the Gas (Safety and Licensing) (LPG Events) Order, 5779-2018

The draft bill seeks to regulate and change certain issues in the gas sector, relative to the current provisions of the Gas Law. The draft includes issues such as: the addition of reporting obligations for gas facilities for personal consumption, the determination of conditions in the gas supplier license, pecuniary sanctions for safety violations, the liability of the gas suppliers for agents acting on their behalf, etc.

The draft order seeks to regulate the issue of the handling of and response to gas events, and includes reference to the issue of the telephone response to emergency calls, arrival times, the manner of handling of a gas event and the manner of the subsequent resumption of the gas supply.

## Natural gas operations

Supergas' operations in the natural gas marketing sector is subject to the provisions of the Natural Gas Sector Law, 5762-2002 (the "Gas Sector Law"), which is the principal law regulating the Israeli natural gas sector. The Gas Sector Law prescribes, *inter alia*, that engagement in activities of construction and operation of a transportation system or part thereof, construction and operation of a distribution network or part thereof, and construction and operation of a storage facility, are prohibited, unless done pursuant to a license granted by the Minister of National Infrastructures and in accordance with the conditions thereof.

The Gas Sector Law further prescribes that the following are prohibited from engaging in the sale and marketing of natural gas: (a) a transportation license holder; (b) an electricity supplier.

According to the Gas Sector Law, engagement in the sale and marketing of natural gas does not require a license, but the Minister of Energy may determine, upon the fulfillment of the conditions prescribed by the Gas Sector Law and with the consent of the Minister of Finance and approval by the Knesset's Economic Affairs Committee, that, for a period to be determined, engagement in natural gas marketing will require a license. In April 2013, the Control of Prices of Commodities and Services Order (Application of the Law to Natural Gas and Determination of Control Level), 5773-2013 and an announcement by the Supervisor of Prices at the Ministry of Energy were published, whereby every marketer or anyone that has signed a contract for the marketing or sale of natural gas, is required to report on the profitability and prices of natural gas, once every six months, on the dates and in the manner published by the Supervisor.

## Antitrust – Economic Competition

Since 1999, Supergas has implemented an internal enforcement program in the format defined by the Economic Competition Authority (the "Antitrust Authority" or the "Economic Competition Authority"). Supergas updates the internal enforcement program from time to time and follows the outline defined therein for efficient and effective internal enforcement of the provisions of the Economic Competition Law, 5748-1988 (the "Economic Competition Law"), the regulations and the orders promulgated thereunder. Participation in the program increases the awareness of Supergas' employees and managers as aforesaid of the requirements of the Economic Competition Law and opens up channels of communication between the employees and the senior management of Supergas, and also between them and the officer in charge of internal enforcement of the Economic Competition Law, as appointed by Supergas' management. Beyond the aforesaid, through the enforcement program, Supergas is doing everything in its power to ensure that Supergas, its managers and its employees act and will act in accordance with the provisions of the law, thereby reducing the exposure of itself and its managers and employees to legal proceedings related to this matter. On September 13, 2016, investigators of the Economic Competition Authority arrived at Supergas' offices for the purpose of collecting documents in connection with an investigation being conducted by the Authority, on the suspicion of violation of the Economic Competition Law. On December 31, 2018, the Economic Competition Authority released a public notice whereby it summoned to a hearing, before the filing of an indictment, officers of Amisragas and Pazgas on suspicion that they collaborated to undermine the competitive activity of Kolbogas. The Authority's notice does not ascribe to Supergas involvement in the alleged violations, and no invitation was delivered to Supergas or to any of its officers to a hearing in respect of this matter.

## Standardization and quality control

Supergas markets its products in accordance with various standards that are relevant to the marketing and supply of LPG which are published from time to time by virtue of the Standards Law, 5713-1953. The standards specify technical requirements that apply to products including with respect to product specifications, methods of production, storage, supply, operation etc. Supergas is certified under quality standard ISO 9001-2000, which concerns quality assurance for the production-supporting management processes. Once every six months the Standards Institution of Israel holds an audit of compliance with the procedures and requirements. Supergas has also been certified under safety standard OHSAS 18001. Supergas has systems for quality control, security and quality management in accordance with the requirements of such standards. Compliance with the procedures and requirements is inspected by the Standards Institution of Israel every six months. Supergas has specific employees who are in charge of quality assurance.

## 12.16. Material agreements

### Construction and operation of natural gas distribution networks

In the segment of construction and operation of natural gas distribution networks, Supergas acts through Super NG and Super NG Hadera, which are equally held by Supergas and by Shapir Civil and Marine Engineering Ltd.

In November 2009, Super NG was granted a license for the construction of a natural gas distribution network in the central region and for the operation thereof for a term of 25 years. Under the terms and conditions of the license, Super NG was obligated to invest approx. NIS 160 million in the construction of the distribution network over an 8-year schedule according to the milestones specified in the license, and it will receive its revenues from a one-time connection fee and from the distribution fee tariff according to the size of the customer (the extent of natural gas consumption).

In April 2013, Super NG Hadera was granted a license for the construction of a natural gas distribution network in the Hadera and Valleys region and for the operation thereof for a term of 25 years. Under the terms and conditions of the license, Super NG Hadera was required to invest NIS 217 million in the construction of the distribution network over a 5-year schedule, according to the milestones specified in the license, and it will receive its revenues from a one-time connection fee and from the distribution fee tariff according to the size of the customer (the extent of natural gas consumption).

Super NG and Super NG Hadera have signed contracts with customers for natural gas distribution services. The companies have begun the piping of natural gas to customers and are acting for completion of the planning of segments and continues to develop the construction of the network. In view of bureaucratic and regulatory difficulties which are delaying progress with rollout of the network and the connection of consumers, and in view of the requests of Super NG and Super NG Hadera to update the conditions of the license and the timetables, in May 2018, a call was released by the Ministry of Energy for acceleration of the rollout of the distribution network, aimed at helping the distribution companies complete the rollout of the distribution network. Super NG and Super NG Hadera responded to the call and signed agreements for the outline of development of the distribution networks. Concurrently, Super NG and Super NG Hadera are continuing to act to update the terms and conditions of the license.

The shareholders of Super NG and Super NG Hadera have also provided, according to their holdings, a guarantee in favor of the Natural Gas Authority, in accordance with the terms and conditions of the tender and the license.

## 12.17. Goals and business strategy

Supergas and GES periodically examine their strategic plans and update their goals according to the developments in the markets in which they operate. Supergas seeks to expand the range of energy solutions provided thereby to its customers and to expand and diversify its customers in its operating segments. Supergas and GES also act for the constant improvement of customer service and for strict compliance with safety and environmental protection rules, and also act for the identification of new business opportunities.

## General information about GES

In the sector of treatment of water, wastewater, air, waste, chemicals for industry and environmental protection sector, Granite operates through GES and consolidated companies thereof (the "GES Operations"). GES engages in engineering design, construction and production, operation and maintenance of plants for water filtration and improvement, desalination of seawater and saline wells, pumping stations and water pools, treatment of well water and treated wastewater and treatment of sanitary, industrial, and municipal wastewater. In addition, GES, by itself and thorough its subsidiaries, engages in marketing and development of chemical products for the purpose of metal treatment and protection, water treatment and also in the importation and marketing of oils, adhesives and chemicals for industry.

### 12.17.1. Structure of the competition in the GES Operations and changes occurring therein

GES and its consolidated companies act in this sector through two divisions:

#### The water and wastewater division

The division engages in the production, construction, operation and maintenance of seawater and brackish water desalination plants; wastewater treatment and treated wastewater reclamation; water betterment and wastewater treatment in the industrial sector; water purification and wastewater treatment in the municipal sector; provision of system operation and maintenance services; planning and production of systems for wastewater and water treatment. GES presently operates approx. 110 plants all across Israel.

#### Industrial chemicals division

The division engages in production, importation and marketing of chemicals and finishing processes for metals; chemicals for the preparation of surfaces for painting and industrial paint strippers; implementation of special chemicals for the treatment of water and wastewater, desalination and cooling towers for the municipal and industrial sector; electrochemical coating materials for the high-tech and electronics industries; industrial cleaning materials; special industrial adhesives and lubricants and chemicals for water and an operation of solvent recycling for parts washers.

### 12.17.2. Restrictions, legislation, standardization and special constraints applicable to the GES Operations

See Section 12.28 of this Chapter A.

### 12.17.3. Changes in the scope and profitability of the GES Operations

See Section 3.1 of the Board of Directors' Report. Regarding Zero Waste's winning of a tender for the construction of a facility for waste sorting and recycling and energy production at the Rishon LeZion area, see Section 1.3.6 of Chapter A above.

### 12.17.4. Developments in the markets of the GES Operations or changes in the characteristics of its customers

Recent years have seen a development in the perception of and attitude towards the water and wastewater industry, primarily in view of the increased awareness of the shortage of clean water in various parts of the world, including Israel, alongside technological developments in these fields that led to reduced water treatment costs and a certain saturation in the construction of desalination facilities and water treatment sector in Israel. Over the last year, the problem of Israel's water shortage has reemerged, and the state has begun promoting large desalination projects, including “Sorek 2”, the tender for the construction of which is currently being conducted. It is noted that in Northern Israel, there is still a water shortage, and it appears that several major projects are currently being promoted in this region. In addition, increased regulation and enforcement create opportunities in the wastewater treatment industry.

### 12.17.5. Critical success factors in the GES Operations and the changes occurring therein

#### In the water and wastewater segment

The integration and implementation of advanced water and wastewater treatment methods and technologies, which lead to energetic and operational streamlining, are a factor that affects the production costs in the water and wastewater plants constructed and operated by GES. Such streamlining leads to tenders being won and to engagement in agreements in the water and wastewater segment for the sale and operation of water and wastewater treatment plants, in Israel and abroad.

#### In the chemicals segment

The production and distribution of high-quality chemicals of world leading producers to customers that demand high-quality and not necessarily inexpensive products.

### 12.17.6. Changes in suppliers and raw materials

Several factors, which are specified below, support the continued activity of construction, upgrade, operation and maintenance of plants for the treatment and desalination of wells and for the treatment and purification of wastewater and reclamation thereof for industrial and agricultural use, and possibly even an increase in the use of such means. Thus, such factors include the shortage of drinking water in some areas of Israel, the high costs of the potable water used both for drinking and for industry along with the damage to wells due to the salification and contamination of aquifers in past years and the strict enforcement of the regulation that governs the treatment of municipal and industrial wastewater. For details with respect to raw materials and suppliers, see Section 12.26 of this Chapter A.

### 12.17.7. Key entry and exit barriers of the GES Operations and changes occurring therein

The principal entry barriers in the operations of desalination and treatment of water and wastewater, are the accumulation of proven experience in the construction and operation of similar plants, which is a threshold requirement in most tenders and engagements in the sector, skilled and experienced manpower, including water and wastewater engineers and technicians, and the requirement to have the appropriate contractor licenses required for the purpose of construction of plants of such type.

The principal barriers for exit from this field are the undertakings to complete the construction of plants, the warranty period granted in the framework of the plant construction agreements, and the term of the undertakings under maintenance and operation agreements.

The principal entry barriers in the chemicals sector are the existence of a suitable production facility, which requires approvals by various authorities, chief of which is the Ministry of Environmental Protection, and the knowledge required for the production of the materials, as well as engagements with leading producers in the world for the receipt of intellectual property usage rights for the purpose of producing and supplying ready-made products for sale and distribution.

The principal barriers for exit from this activity mainly pertain to the ending of the lease agreement of the production facility’s premises and the duties imposed in connection with the requirements of the law and the Ministry of Environmental Protection in the vacating of land on which operations of such type were conducted.

### 12.17.8. Structure of the competition in the GES Operations and changes occurring therein

For details with respect to the structure of the competition in the GES Operations and changes occurring therein, see Section 12.21 of this Chapter A.

## 12.18. Products and Services

### 12.18.1. Water and wastewater segment

The primary systems used by GES for the treatment of water and wastewater are: membranal high-pressure systems for the separation of salts, systems of filtration and purification through chemicals and various filters, anaerobic and aerobic systems for the treatment of industrial and municipal wastewater and systems for the treatment of sewage sludge. The systems include dosage, command and control units.

GES offers its customers a broad range of water and wastewater treatment systems and solutions, the principal of which are: Brackish water and seawater treatment systems; wastewater treatment systems; well betterment and improvement plants; water treatment methods based on diverse technologies; treatment of steam systems and energy centers; plants for the desalination of treated wastewater to irrigation standard.

GES offers customers project supervision and management, including construction, professional support and backup services, which include the instruction of operators at the customer's site, professional advice and consultation in the operation of the project, maintenance and operation services, monitoring and supervision for the purpose of performing process optimization and the performance of periodic surveys and ongoing maintenance of the project.

### 12.18.2. Chemicals segment

The principal services and products of GES in the chemicals segment include surface treatments, adhesives and sealing materials, chemicals for electrolytic coating and printed circuit boards, special industrial lubricants, industrial maintenance products, recycling of industrial cleaning materials and chemicals for water.

## 12.19. Customers

GES's customers include water corporations and local authorities, government-owned companies and industrial companies.

## 12.20. Marketing and Distribution

GES invests great efforts in diverse marketing activities in each of its operating segments. Such marketing activities include the following:

1. Domestic sales agents – some of GES's people are domestic sales agents who are on the ground on a daily basis in order to identify new customers, address the needs of existing customers, and market GES's products.
2. Focused sales efforts overseas, particularly targeting suitable markets both geographically and vis-à-vis potential customers who are engaged in relevant business.
3. Distributors – in the chemicals segment, there are some 10 large distributors (mostly stores) nationwide, through which GES markets some of its products.
4. Management and maintenance of informational websites at the addresses: www.ges.co.il and www.ges-texma.co.il, which include an extensive description of the company's operations and products and contact information.

5. Activity amongst professionals – GES maintains relations with professionals in the context of exhibitions (in Israel and abroad), professional conferences, training sessions, seminars, etc.
6. Tenders – GES has a system for identifying tenders and requests for proposals for the performance of projects relevant to its operating segments, including the preparation of tender bids and proposals for such requests.

In addition, GES conducts export activities in all of its operating segments. Most of GES's products marketed abroad are marketed under the "GES" brand.

## 12.21. Competition

Competitors in the operating segments of GES are a large number of companies engaged in the construction of systems for water purification and wastewater treatment, as well as companies engaged in the manufacture and import of chemicals. Competition exists both in the search for and identification of new customers and in the provision of high-quality services in all of GES's operating segments. Competition revolves around prices, service quality, financing terms and technical specifications. The operations of the divisions of GES in the fields of projects and operation have a large number of competitors, including: Nirosoft, Rimon, E.L.D., Elco, Winter, Odis, IDE, Palgey Maim, Lesico, Shtang, Mekorot Development, T.G.L., Minrav, Baran, Shikun & Binui Water, EPT, Hutchison, Ludan, Elad, Jetline, D.S. Service Provision and more.

In the chemicals segment, each of the division's product lines has several significant competitors that produce and/or import alternative products to the division's products, such as: Amza and Elad Technologies in chemicals, Nalco and YWCT in water chemicals, Layogev, Pronat and Rotal in adhesives, and the large energy companies (Paz and Delek) in lubricants.

GES is handling the competition via, *inter alia*, the implementation of new, advanced technologies, analyzing and understanding customer needs and professionalization which enable the offering of a quality, advanced and efficient product in comparison to parallel products. This is performed through the engagement with new suppliers in existing markets, the development of new technologies through new suppliers and the implementation of advanced technologies of existing suppliers.

## 12.22. Production Capacity

GES's production layout is centered in two sites: Akko South and Askar (in the Akko area). In addition, GES uses outside contractors for the production of water facilities at production sites of such contractors and through manpower on their behalf which is supervised by GES employees.

### Water and wastewater segment

The production layout responsible for the construction of water and wastewater treatment systems is based in the Askar site, which is situated in the municipal area of Regional Council Matteh Asher. GES has the capacity to simultaneously produce a number of plants. The production may be carried out independently, as was done in the recent period for reasons of streamlining through subcontractors, with supervision thereof.

### Chemicals segment

The Akko South site, which is situated in the municipal area of the Akko Municipality, hosts the production layout responsible for the production of special chemicals for the treatment of metals, water, wastewater, desalination, and cooling towers for the municipal and industrial sectors.

All finished products in the chemicals segment are manufactured to order. Under GES's policy, the production site does not produce a regular inventory of finished materials, but rather per customers' orders.

GES uses approx. 60% of the production potential of the production site. The potential production capacity is approx. 5,000 tons of various types of chemicals, assuming that production work is performed in two shifts per 24 hours, with work presently performed in one extended shift.

## 12.23. Fixed Assets, Real Property and Plants

GES and its wholly-owned subsidiary GES Plant Operation Ltd. have several water and wastewater treatment plants in the framework of BOT agreements with the private and municipal sectors. GES has machines and equipment that are used to produce chemicals and an evaporation plant for the treatment of industrial wastewater, which are situated in the Akko South production site. GES's production layout is centered in two sites: Akko South and Askar (in the Akko area), under lease agreements from a third party.

## 12.24. Intangible Assets

### 12.24.1. Trademarks

GES has a trademark on goods and services supplied thereby which include: the provision of environmental protection solutions, seawater and brackish water desalination, wastewater treatment and treated wastewater reclamation, water betterment and implementation of special chemicals for water treatment.

The registration of the trademarks is highly important, since they serve as means for the identification of GES's products in its business field with GES.

### 12.24.2. Distribution rights

In the chemicals segment, GES has a large number of marketing and distribution agreements with companies in Israel and around the world which are leading in their fields. Under such agreements, GES is the official representative in the marketing, production and import of these companies in Israel.

### 12.24.3. Marketing and distribution Agreements

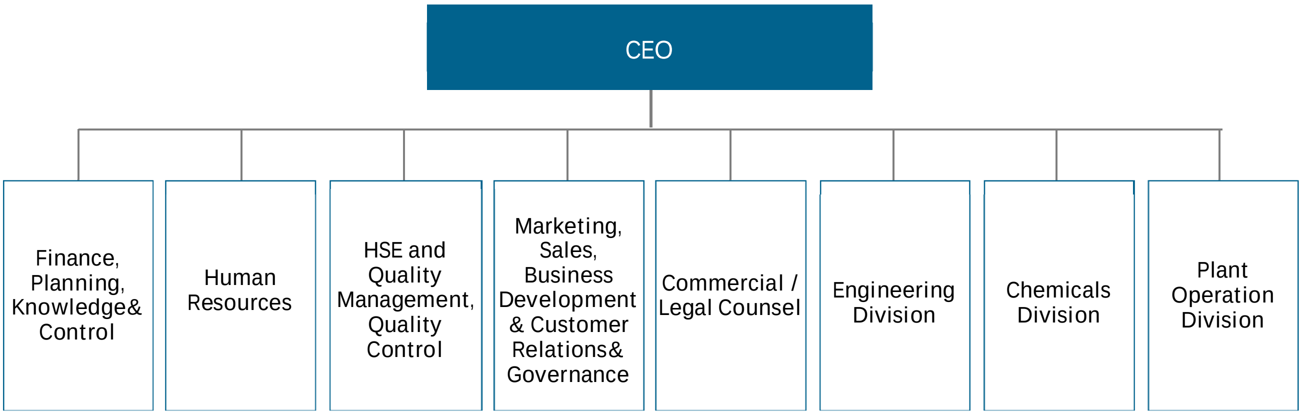
The chemicals segment has a large number of marketing and distribution agreements with companies in Israel and around the world which are leading in their fields. Under such agreements, GES is the official representative in the marketing, production and import of such companies in Israel.

## 12.25. Human Capital

As of December 31, 2018, GES employs 200 employees.

### 12.25.1. A description of the organizational structure of GES follows:

### 12.25.2. Breakdown of employees by position:




The breakdown of GES's employees is detailed below:

| Position/Division | Number of Employees December 31, 2018 | Number of Employees December 31, 2017 |
|---|---|---|
| GES Management | 25 | 23 |
| Water and Wastewater Division | | |
| Production and operation | 83 | 78 |
| Marketing and sales | 21 | 17 |
| Chemicals Division | | |
| Production and operation | 33 | 30 |
| Marketing and sales | 38 | 40 |
| Total employees | 200 | 188 |

### 12.25.3. Benefits and the nature of employment agreements

GES employs permanent employees, 31 of whom are employees who are subject to special collective bargaining agreements. GES is not dependent on any particular employee.

The other employees of GES are employees employed under personal employment agreements, temporary employees employed under the rules of the special collective bargaining agreement and the general labor law, seasonal employees, and contractor employees engaged under agreements with employment agencies.

The permanent, monthly and temporary employees are divided as follows:

Permanent employees are divided into two groups as follows:

1. Permanent employees employed under a collective bargaining agreement – As of the Report Date, this group consists of 31 employees (Generation A and Generation B). The terms and conditions of their employment are provided by a collective bargaining agreement of 1988, which is valid to date. GES employees working in the production department, workshop and junior clerks (according to an agreed list of professions) are subject to the terms and conditions of such collective bargaining agreement.
2. Permanent employees under personal agreements – As of the Report Date, this group consists of 169 employees. Standard employment agreements apply between GES and such employees which provide, in most cases, the employee's salary, working hours, social benefits, such as managers' insurance, provident funds, pension funds, advanced study fund, entitlement to leave, recuperation pay and sick leave,

participation in mobile telephone expenses, reimbursement of *per diem* expenses, the period of prior notice for resignation and for dismissal, confidentiality and non-competition. Most of the employees are employed based on an overtime-inclusive salary. About 50% of the employees receive a company vehicle for their use for the purpose of fulfilling their duties. Salespersons are granted quarterly incentives. All personal contracts include an express provision as to the application of Section 14 of the Severance Pay Law, 5723-1963, and the balance is covered by full severance pay contributions.

In addition, GES has agreements in place with several employment agencies for the placement of temporary professional employees. The temporary employees are usually employed for specific purposes and for predefined time periods.

### 12.25.4. Liabilities for the termination of employment relations

The liabilities of GES and its subsidiaries to employees for the termination of employment relations are covered by current payments to insurance companies for managers' insurance policies, pension funds and provident funds, and by a provision in the Group's financial statements reflecting liabilities thereof which are not so covered.

## 12.26. Raw Materials and Suppliers

The main raw materials used by GES for the water and wastewater operation are: finished equipment, which includes pumps, membranes, pressure cabins, tanks and chemicals for the operation of water and wastewater plants. Such raw materials and equipment items are acquired from leading companies in the world. All of the purchased raw materials and parts are checked by a quality control lab and the Quality Assurance Department of GES according to international standards. In some cases, equipment items are manufactured specifically for GES according to defined requirements for specific projects, especially when particularly good abilities and quality of materials are required according to the customer's demand. Supply times of such equipment range from one month to a period longer than one year. Substantial raw materials are mainly purchased from local suppliers, and parts are also imported, mainly from the U.S., Canada, Korea and European countries.

In the chemicals' operations, GES uses numerous raw materials for its and its customers' purposes, the principal ones of which are: 60% nitric acid and technical hydrochloric acid. These raw materials are purchased chiefly from the local market. All of the purchased raw materials are checked by a quality control lab and the Quality Assurance Department of GES. Supply time of the raw materials in the chemicals segment is immediate when sourced locally and around two months when imported. Most of the imported raw materials are purchased from U.S. and European suppliers.

## 12.27. Environmental risks and their management

12.27.1.GES's operations of industrial and sanitary wastewater treatment, recycling of materials and water treatment and betterment, and production and distribution of chemicals (including adhesives, lubricants, oils) are subject to provisions that pertain to environmental protection and which are relevant to the operating segment, as well as to aspects of health and safety. Operations in such fields are performed under the supervision of the Ministry of Health which performs routine tests to examine the quality of the water generated in the treatment plants and in the desalination plant, and under the supervision of the Ministry of Environmental Protection, the Ministry of Health and the Water Authority over the quality of the wastewater treatment in the treatment plants and compliance with the production permit. In addition, in the context of this activity, supervision is exercised also by government authorities such as the Ministry of Environmental Protection, the Water Commission and the Water Economy Administration, the local authorities and the water and sewage corporations and relevant business licensing authorities. Under various provisions of the law and permits issued thereto, GES is obligated to comply with stringent standards with respect to the drinking water desalinated in its plants and the treated wastewater discharged into streams and into the sea or used in agriculture.

GES treats industrial wastewater created in the production of chemicals at GES's Akko South production site in full and in accordance with the provisions of the law and the requirements of the Ministry of Environmental Protection and the Municipal Association for Environmental Protection.

The implications of failure in the treatment of byproducts (such as sewage sludge and brine) created in the context of GES's operations constitute a risk of environmental hazard and soil contamination. Deviation from the provisions of the law and the requirements of the Ministry of Environmental Protection and the Municipal Association for Environmental Protection might lead to health damage or environmental damage, including the supply of substandard drinking water, harm to agricultural crops and soil contamination. GES also handles and trades in poisonous and hazardous substances within its business operation of manufacture and distribution of products in the segment of water and industrial chemicals and within the maintenance of GES's water and wastewater treatment plants. GES has valid poison permits and a hazardous substances certification. GES's chemicals production site includes a wastewater treatment plant. The plant treats the wastewater of the production site and the wastewater of customers transported to GES's plant with the approval of the Ministry of Environmental Protection.

Furthermore, since a large part of the GES Operations is based on the use of chemicals, GES is supervised by the Ministry of Environmental Protection and the municipal authorities and is committed to the protection of the environment and to working in accordance with the environmental standards, laws and regulations of the Ministry of Environmental Protection and the relevant municipal associations, including the provisions of the Hazardous Substances Law.

### 12.27.2. GES's policy on environmental risk management

GES strictly ensures to fully comply with all of the requirements of the provisions of the law pertaining to environmental protection. GES regularly implements Environmental Protection Standard ISO 14001 and is annually certified by the Standards Institution of Israel. GES implements an internal environmental enforcement program, under which periodic inspections are performed in order to ascertain that the company's operations in the various sites comply with the requirements of the various environmental protection laws and the business licenses applicable to the various plants operated by GES. GES conducts occupational medical and environmental monitoring on an annual basis to ascertain that there are no deviations from the level permitted under the standardization.

Once every three years, GES conducts a job safety analysis (JSA) in all of the company's sites and carries out the remedial actions required pursuant to the analysis.

GES employs a full-time safety and environmental protection manager, whose responsibility includes management, monthly supervision of sites, training and the organization of emergency teams for an environmental incident, investigation of incidents and implementation of remedial actions, in order to reduce the exposure to environmental risks. GES annually carries out occupational medical check-ups for employees who are exposed to hazardous substances and to noise in their work, in accordance with the provisions of the law. The check-ups for the employees and the medical follow-up are performed by the occupational clinic of the Rambam Hospital.

In the framework of GES's operations both in the water and wastewater treatment segment and in the chemicals production and distribution segment, use is made of materials defined as hazardous substances under appropriate licenses and poison permits issued for the purpose of water and wastewater treatment and also due to their being a raw material for the production of chemicals, which are also defined as hazardous substances. Failures in the production, operation, storage, use or transportation of such substances might lead to environmental hazards or to accidents, such as: flare up, air pollution, soil contamination and more. The GES

Operations in such fields is performed under an environmental enforcement program in which exposures have been and are mapped, and based thereon, emphases are made and preventive action is taken and considerable management resources and input are invested.

## 12.28. Restrictions on and Supervision of the GES Operations

### 12.28.1. Water and wastewater

This operation in Israel is subject to various legal provisions that regulate environmental protection and the quality of the water and wastewater treated by GES in the various plants, chief of which are the Water Law and the regulations thereunder, the Prevention of Marine Pollution by Land-Based Sources Law, the Water Regulations (Prevention of Water Pollution – Use and Disposal of Sewage Sludge), the People's Health Ordinance and the regulations thereunder, the Water and Sewage Corporations Law and their rules, the Hazardous Substances Law, the Environmental Protection Law (Emissions and Transmissions to the Environment – Register and Reporting Duties) and more. Such laws, ordinances and regulations prescribe a line of provisions pertaining to the protection of water sources and the prevention of water contamination, the quality of the water and treated wastewater produced at the plants, the types of treated wastewater, the manner of disposal of the sewage sludge and wastewater in various cases, the hazardous substances that are used and the manner of storage thereof, the emission of contaminators from the GES plants and more. In addition to the aforesaid, GES operates in accordance with and by virtue of certificates, permits and specific instructions by the various authorities.

### 12.28.2. Chemicals

This operation is subject to various legal provisions that regulate environmental protection, chief of which is the Hazardous Substances Law and the regulations thereunder, the Clean Air Law, the Environmental Protection Law (Emissions and Transmissions to the Environment – Register and Reporting Duties) and more. Such laws, ordinances and regulations regulate the manner of preventing the emission of contaminators from GES's production plants and the reporting of such emissions, procurement, storage, production and trade in the hazardous substances distributed by GES and more. In addition to the aforesaid, GES operates in accordance with and by virtue of certificates, permits and specific instructions by the various authorities.

GES holds all of the licenses and permits required by law, as aforesaid.

## 12.29. Granite Segment – other operations

Other than the operations described above, Granite is a 50%-partner in a limited partnership that has built and operates a unique tourist attraction known as "Mini Israel", which presents miniature models of renowned Israeli sites.

## 12.30. Goals and business strategy

See Section 12.7 of this Chapter A above for details.

# 13. The Sonol Segment – Discontinued Operations

## 13.1.

Until July 2016, the Group operated through Sonol in two principal business sectors: direct marketing and fueling and retail complexes. The Group, through Granite Hacarmel, held 100% of the rights in Sonol.

## 13.2.

In accordance with the Group's strategy of focusing on the core areas of the real estate business while regularly examining its holdings that are not within its core business, on April 14, 2016, Granite Hacarmel entered into a transaction for the sale of all of its holdings (100%) in Sonol to Israel Oil & Gas Fund L.P., a limited partnership incorporated in Israel, the general partner of which is controlled by Mr. David Weissman, in consideration for a total sum of NIS 363.5 million. The provisions of the agreement determined that the majority of the consideration would be paid on the transaction's closing date (subject to certain adjustments stipulated in the agreement), and part thereof will be paid on a date subsequent to the transaction's closing date. The transaction further determined that from the transaction's closing date and for a 4-year period, the Company and Granite Hacarmel will not compete with Sonol's business. This obligation does not apply to the operations and business plan of the Supergas Group.

On July 24, 2016, in view of the fulfillment of the conditions precedent specified in the agreement, the transaction was closed, without material change. On the closing date and thereafter, the purchaser paid such part of the consideration as was scheduled for payment on the closing date. For further details, see the Company's reports of June 18, 2015, October 26, 2015, February 2, 2016, April 14, 2016, June 19, 2016 and July 24, 2016 (Ref.: 2015-01-050991, 2015-01-141945, 2016-01-021562, 2016-01-048793, 2016-01-052239, and 2016-01-088873, respectively), which are included herein by way of reference.

## 13.3.

In view of the sale of Sonol and in accordance with GAAP, as of the transaction's closing date, Sonol is presented in the Financial Statements as discontinued operations. For further details, see Note 8 to the Financial Statements.

# PART FIVE: ADDITIONAL OPERATIONS

## 14. Azrieli Group - Additional Business

The Group has various operations which are not included in the operating segments described above, and do not meet the quantitative threshold for presentation as reportable segments in the Financial Statements. These activities comprise mainly the following:

### 14.1. The e-commerce business

On June 2, 2016 the Company closed a transaction for the purchase of an e-commerce business from Buy2 Networks Ltd. This business is currently operated by Azrieli E-Commerce (formerly Netex New Media Ltd.).

This company has been operating an e-commerce website since 2010, which until February 2017operated under the brand name “Buy2”. As of February 2017, this website was re-launched by Azrieli E-Commerce under the brand name “Azrieli.com” at the address www.azrieli.com (“Azrieli.com” or the “E-Commerce Website”)

Azrieli.com offers internet users a range of products and services, which are supplied by various businesses of various areas, including electricity and electronics, fashion, home and garden, parents and children, and more. Furthermore, the E-Commerce Website grants internet users benefits that vary from time to time, including free shipping and express deliveries to the customer’s home and payment in installments.

Azrieli.com facilitates a comprehensive solution of online marketing and sale for businesses that seek to sell products and services at Azrieli.com, including the storage of products in a central logistics center, the sale, supply and distribution of products to the customer’s home, through third parties. Azrieli E-Commerce works on the development of long-term relations and work interfaces with the businesses active on Azrieli.com, aiming to retain and increase the cooperation. Alongside the sale of the businesses’ products, Azrieli E-Commerce selectively purchases products it sells on the E-Commerce Website and supplies such products to customers by means of third parties.

In addition to the aforesaid business, as part of Azrieli.com’s operations, the website displays a range of domestic tourism and foreign tourism (an operation in cooperation with a third party). Azrieli E-Commerce employs some 80 employees and its offices are located at the industrial zone of Hod HaSharon.

General description of the E-Commerce Business

Recent years saw changes in the shopping habits of Israeli consumers alongside technological changes that enable online shopping and render a larger range of online-offered products and services available to the consumer. Online shopping enables quick and convenient service which is customized to the consumer’s consumption habits and preferences. In recent years, the e-commerce business in Israel has been developing at an accelerated pace and this sector is expected to double by 2021 and reach approx. NIS 15 billion per year and expected to represent approx. 12% of the Israeli retail market in that year[37].

Concurrently with the increase in the range of products purchased online by Israeli consumers, there is a noticeable increase in online shopping on international websites (such as eBay, AliExpress, Next and Amazon). In the estimation of Azrieli E-Commerce, the volume of the activity is affected by the volume of private consumption and changes in Israeli consumers’ use of the internet. The growing use of the internet by means of mobile devices, such as tablets and cellular telephones, may contribute to greater exposure and availability of e-commerce services.

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[37] Geocartography, data taken from a comprehensive study of the trade sector in Israel, March 2018 , conducted for Azrieli Group.

Entry and exit barriers

The setup of a line of suppliers, while developing ties and retaining the relationship therewith, may serve as an entry barrier to new players in the short-term and the mid-term. Furthermore, the development of the technology required for the operation of the e-commerce business in similar form and scope and the need to generate a high rate of user traffic may serve as entry barriers to new players, *inter alia*, due to the great importance of the website's reliability and the high costs involved in the recruitment of user traffic. Moreover, the building of a registered user database, including the ability of mailing thereto, also serves as an entry barrier.

Exit barriers may stem from the need to convert a complex set of agreements with various suppliers, and also from the need to preserve the brand name and its credibility among the public of customers.

Restrictions on and supervision of the operations

The e-commerce operations are subject to various laws, such as: the Consumer Protection Law, 5741-1981 and the regulations thereunder, the Privacy Protection Law, 5741-1981, the Communications Law (Telecommunications and Broadcasting), 5742-1982, and the Debit Cards Law, 5746- 1986, which will be revoked upon the taking effect, in 2020, of the Payment Services Law, 5779-2019 ).

Furthermore, since purchases on Azrieli.com are made by means of credit cards, various provisions and restrictions required by the credit card companies apply, including security standard PCI.

Competition

The e-commerce market is a competitive market and includes competition by international websites that offer shipping to Israel (such as eBay, Amazon and AliExpress) along with Israeli e-commerce websites, such as Walla! Shops, Shufersal, GetIt, as well as the websites of other companies on which such companies directly offer their products for sale.

In the estimation of Azrieli E-Commerce, the success factors in the e-commerce operations are, *inter alia*: (a) The offering of high-quality products and services on attractive terms to internet users; (b) Engagement with reliable businesses, in a blend addressing a broad array of internet users; (c) User traffic and the size of the mailing list; (d) Reliable and available customer service; (e) Technological improvements and innovations that contribute to the improvement of the quality of the website's applications, with an emphasis on the devising of simple and user-friendly interfaces; (f) Compliance with supply time obligations, which contributes to the increase of the number of repeat purchases by Azrieli.com customers.

*The Company's estimations with respect to the e-commerce operations, including the development of such operations in Israel, the increase in online purchases and the volume of operations in the segment constitute forward-looking information, within the meaning of this term in the Securities Law, which is based on publications in the field and subjective assessments by the Company's management as of the Report Date. There is no certainty that such estimations will materialize, in whole or in part, and they may also materialize in a materially different manner, inter alia due to factors that are beyond the Company's control, including changes in market conditions, growing competition and deterioration in the economic situation, which might affect customers' consumption habits.*

## 14.2. Investments in financial assets available for sale and other investments

### 14.2.1. Investment in Leumi Card

On May 26, 2008, the Company invested the sum of NIS 360 million, as a passive financial investment, in Leumi Card (total investment net of a dividend and consideration from the sale of Visa Europe Ltd.[38] that were received, as of the Report Date, is NIS 232 million), and in consideration for which Leumi Card issued shares to the Company which represented 20% of the issued and paid-up capital of Leumi Card (post money and on a fully diluted basis) (the "Investment Agreement").

For further details regarding the Investment Agreement, see Section 14.2.1 of the Company's periodic report for 2017, which is included herein by way of reference.

On February 25, 2019, a transaction for the sale of all of the holdings of the Company and Bank Leumi Le-Israel Ltd. ("Bank Leumi") in Leumi Card to Warburg Pincus Financial Holdings (Israel) Ltd., a corporation controlled by the Warburg Pincus investment fund, was closed. For further details regarding the transaction, see Section 1.3.9 above. Upon the closing of the transaction, the Investment Agreement was terminated.

The Company's investment in Leumi Card is presented on its books as an asset held for sale within the current assets, according to GAAP. The value of the Company's investment in Leumi Card as of December 31, 2018, was set according to the discounted net consideration excepted to be received from the sale as aforesaid, at a total of approx. NIS 450 million.

Dividend policy in Leumi Card

The dividend distribution at Leumi Card is subject to the provisions of the Companies Law and the directives of the Supervisor of Banks, including compliance with capital adequacy restrictions mandated by the Basel Directives. According to the dividend distribution policy document, which was updated and approved by Leumi Card's board of directors, the following dividend distributions were carried out during 2018 until the Report Release Date: ,

| Distribution resolution date | Payment date | Total distribution amount (NIS in millions) | The Company's share of the total distribution amount (NIS in millions) |
|---|---|---|---|
| 19.2.2018 | 4.3.2018 | 50 | 10 |
| 9.8.2018 | 16.8.2018 | 100 | *20 |
| 11.11.2018 | 14.11.2018 | 58 | *12 |
| 24.2.2019 | 24.2.2019 | 400 | *80 |

* According to the agreement for the sale of the Company's holdings in Leumi Card, as specified in Section 1.3.9 of Chapter A above, the consideration from the sale decreased by the amount of the dividend paid.

Loyalty Program

On May 26, 2008, the Company entered into a cooperation agreement with Leumi Card for the establishment of a program for the benefit of customers of the commercial centers and malls owned by the Company and/or affiliates of the Company, whose members would hold a Leumi Card card conferring special benefits and services (the "Loyalty Program Agreement").

[38] For details about the disagreement between the Company and Bank Leumi and the resolution thereof, in respect of the sale of Visa Europe Ltd., see Note 11B(2) to the financial statements.

The Loyalty Program Agreement regulates the relationship between the parties, and, *inter alia*, sets forth provisions with regards to the terms of the loyalty card to be issued to the customers of the commercial centers and malls of the Company and its design, including the Company's rights to the loyalty program trademark and the member database, and registration thereof in its name.

On January 7, 2010, the Company entered into a licensing agreement with Leumi Card for the use of trademarks, whereby the Company granted Leumi Card an exclusive license to use all of the trademarks registered in the Company's name in connection with the "Multi Azrieli" mark, in connection with a loyalty program of same name.

The license is effective throughout the term of the Loyalty Program Agreement and subject to the conditions thereof. During 2011, the Company registered the "Multi Azrieli" trademark.

In the agreement, the Company undertook to employ a management team to manage the Program's activities throughout the term of the agreement, at an annual cost that shall not exceed the amount of NIS 250,000, to be financed by Leumi Card. In addition, the Company neither has had, nor expects to have any revenues or benefits in connection with the Loyalty Program Agreement. To the best of the Company's knowledge, as of the Report Date, the Loyalty Program comprises approx. 140,300 valid loyalty cards, out of, to the best of the Company's knowledge, approx. 2.65 million valid credit cards that are held by Leumi Card customers.

The loyalty card provides discounts in some of the chains which have presence in the Group's malls, and at the parking lots thereof. The Loyalty Program Agreement and the license agreement for use of trademarks as aforesaid, remained in effect also after the closing of the transaction for the sale of Leumi Card.

Developments during the Report Period

For details regarding the closing of the transaction for the sale of Leumi Card, see Section 1.3.9 above.

For further details regarding regulation in connection with Leumi Card, see Section 14.2.1 of the Company's periodic report for 2017, included herein by way of reference.

### 14.2.2. Investment in Bank Leumi

On April 30, 2009, the Company acquired from third parties, unaffiliated with the Company, as a passive financial investment, ordinary shares of Bank Leumi, a banking corporation whose shares are listed on TASE, which represented approx. 4.8% of the issued and paid-up share capital of Bank Leumi, in consideration for a sum total of approx. NIS 742 million. During 2016-2018 and up to the Report Release Date, the Company disposed of some of its holdings in Bank Leumi for a total sum of approx. NIS 463 million, and its current holding represents approx. 3.05% of Bank Leumi's issued and paid-up share capital (as of the Report Release Date, the total investment net of a dividend that was received and consideration from sales is approx. NIS 140 million). The value of the Company's investment in Bank Leumi as of December 31, 2018 was approx. NIS 1,218 million. The Company's investment in Bank Leumi is presented in its books as a financial asset available for sale in accordance with GAAP.

For details on the disagreement between the Company and Bank Leumi, and the resolution thereof, with respect to the sale of Visa Europe Ltd., see Note 11B(2) to the Financial Statements.

In 2018, the Company recorded a comprehensive profit (before tax) of approx. NIS 86 million due to this investment. For details, see Section 3.2.1 of the Board of Directors' Report.

On the date of the acquisition, on April 30, 2009, the share price was 1,055 (in *Agorot*). As of December 31, 2018 (the last trading day of the year), the share price was 2,260 *Agorot*, whereas at the close of trading on March 19, 2019, the share price was 2,479 *agorot*.

On March 29, 2017, the Bank's board of directors approved a dividend distribution policy, beginning on the release date of the financial statements for Q1/2017. Pursuant to the said policy, the bank will distribute in each quarter a dividend equal to 20% of its net profit according to the bank's financial statements for the previous quarter and subject, *inter alia*, to the Bank's meeting its capital adequacy targets even after the distribution of dividend. On November 20, 2017 the board of directors of Bank Leumi approved a modification to the dividend distribution policy, from 20% each quarter to up to 40% in each quarter, of the net profit for that quarter, beginning with the profits of Q3/2017. In 2018, Bank Leumi distributed a dividend to its shareholders in the amount of approx. NIS 1.4 billion, with the sum of the dividends received by the Company in respect of such distribution is approx. NIS 49 million as specified below:

| Distribution resolution date | Payment date | Total distribution amount (NIS in millions) | The Company's share out of the total distribution amount (NIS in millions) |
|---|---|---|---|
| 5.3.2018 | 28.3.2018 | Approx. 342 (approx. NIS 0.22 per share) | Approx. 12 |
| 23.5.2018 | 19.6.2018 | Approx. 292 (approx. NIS 0.19 per share) | Approx. 10 |
| 13.8.2018 | 6.9.2018 | Approx. 361 (approx. NIS 0.24 per share) | Approx. 13 |
| 12.11.2018 | 10.12.2018 | Approx. 375 (approx. NIS 0.25 per shares) | Approx. 14 |
| 6.3.2019 | 3.4.2019 | Approx. 275 (approx. NIS 0.18 per share) | Approx. 9 |

Bank Leumi's financials are publicly posted on the distribution website of the ISA at: www.magna.isa.gov.il and on the TASE website at www.tase.co.il.

### 14.2.3. Investments in high-tech start-up companies and investment funds

As of December 31, 2018, the Company has invested in a startup companies and in two investment funds, which are presented at fair value in the sum of approx. NIS 9 million, compared with a fair value in the sum of approx. NIS 17 million as of December 31, 2017.

### 14.2.4. Holdings in other foreign companies

The Company holds approx. 3.8% of the issued and paid-up share capital of Health and Fitness East Med. B.V., which operates the "Holmes Place" chain of fitness centers in Greece.

# PART SIX: MATTERS COMMON TO THE GROUP'S ACTIVITIES IN ALL OF ITS OPERATING SEGMENTS[39]

## 15. Fixed assets, land and facilities

The Company's offices are situated on the 48th floor and part of the 33rd floor of the Round Tower in Azrieli Center in Tel Aviv. The Company leases its offices, a gross area of 2,055 sqm, from Canit Hashalom for a long-term period, for immaterial amounts.

The Group has no material fixed assets except for its offices.

The fixed assets of Palace Tel Aviv are primarily a building that holds the LTC and recuperation units, see Section 11.1 of this Chapter A.

The fixed assets of Palace Modi'in are primarily the LTC and recuperation units.

Supergas' main fixed assets are equipment that is loaned to its customers to be used for LPG supply, such as: stationary or portable gas tanks, meters, regulators and other gas equipment which is installed at Supergas' customers (both the domestic customers and the commercial and institutional customers). For the most part, upon expiration of the engagement the customer is required to return the equipment loaned thereto to Supergas.

## 16. Intangible assets

The primary trade mark owned by the Company and the Group companies (excluding Granite and its subsidiaries), is a designed mark which includes the inscription "Azrieli Group", and the Group's logo:

As of the Report Release Date, the Company owns registered trademarks, including in respect of new properties, such as the trademarks of the Group's senior housing chain – Palace Senior Housing, and the trademarks of the E-Commerce site launched by the Company in February 2017 – Azrieli.com. Furthermore, the Group has submitted additional applications for the registration of trademarks in respect of properties under construction which are under review and registration. The Group has also registered trademarks of the sphere shape that appears at the entrance of some of the Company's malls, and it also owns the Multi Azrieli trademark. Registered trademarks are valid for 10 years and can be renewed, per the Company's decision, for additional periods of 10 years each, without limit, subject to the payment of a renewal fee.

[39] This part "Matters Common to the Group's Activities in All of its Operating Segments" does not include the operating segment of Granite Hacarmel and companies controlled thereby and the e-commerce business, unless otherwise expressly stated.

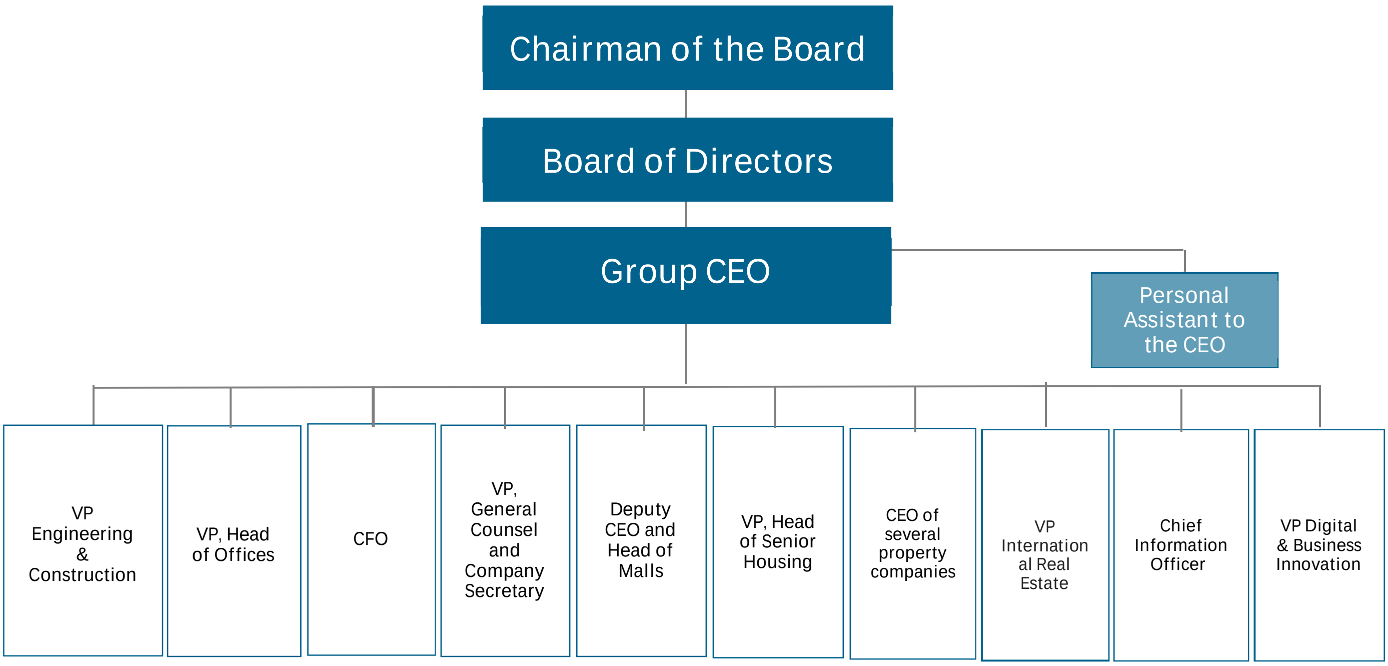
# 17. Human capital

## 17.1. General

The Company places special emphasis on the quality of human capital, particularly at the Company's management level, by hiring a professional workforce with vast knowledge and experience in a variety of fields which are required within the framework of the Company's operating segments. Most of the Company's employees, mainly at its management level, have significant seniority in the Company, and vast experience in its operating segments. Unless otherwise noted, the specification in this Section does not include reference to human capital aspects of the Granite Segment. (For details regarding the human capital in the Granite Segment, see Sections 12.12 and 12.25 of this Chapter A), regarding the senior housing segment (see Section 11.1 of this Chapter A) and the e-commerce business (see Section 14.1 of this Chapter A).

## 17.2. Organizational structure and workforce

The diagram below describes the Group's organizational structure as of the Report Release Date:




As of December 31, 2018, the Group companies employ 341 employees. The segmentation of the employees in the main segments is detailed below:

| Department | Number of Employees as of December 31, 2018 | Number of Employees as of December 31, 2017 |
|---|---|---|
| Management Headquarters* | 63 | 60 |
| Commercial Centers and Malls Segment | 179 | 170 |
| Office and Other Space for Lease in Israel Segment | 99 | 89 |
| Total | 341 | 319 |

*One employee from the management headquarters is attributed to the income-producing property in the U.S. segment and one employee from the senior housing segment.

**For details with respect to all employees of senior housing segment, see Section 11.1 of this Chapter A.

The Group's management and headquarters employs 63 employees, including the Group's CEO, the Deputy CEO and Head of Malls, CFO, VP, General Counsel and Company Secretary, VP and Head of Offices, Overseas Business Development Manager, VP, Head of Senior Housing, VP Engineering and Construction, Chief Information Officer and VP Digital & Business Innovation. The members of the Group's managerial headquarters have considerable managerial experience, and some of them have been by the Group's side for many years. The increase in the number of employees relative to the previous year is attributed to the growth in the Company's real estate business. 179 employees are employed in the Group's retail centers and malls segment, of whom 163 work for the management and maintenance teams of the retail centers and malls engaged in the current management of the retail centers and malls, and 16 provide marketing services to all of the Group's retail centers and malls.

99 employees work in the office and other space for lease in Israel segment, of whom 95 work for the segment's management and maintenance teams engaged in the current management of the offices, and 4 engage in the provision of marketing services.

As of the Report Date, the income-producing property in the U.S. segment is managed by the Company's headquarters and the Overseas Business Development Manager and management services and other services are provided to the Group in this segment by local professional management companies, as of the Report Date.

As of the Report Date, there are, between the Company and the Group companies, cooperation and agreements in connection with the provision of management services between themselves, including, *inter alia*, financial advice, strategic advice and current management advice, in consideration for a monthly payment. In addition, there are management agreements with the Group companies which derive, in part, as a percentage of such company's total expenses. The total payments that were made between the Group companies (including management agreements between subsidiaries of Granite Hacarmel and Canit Hashalom) for these management services, in 2017 and 2018, amounted to the sum of approx. NIS 52 million and approx. NIS 56 million, respectively.

## 17.3. Changes in senior officers in the corporation

In October 2017, Mr. Yuval Bronstein, the Company's CEO at that time, gave notice of the termination of his office on December 31, 2017. On October 19, 2017, the board of directors appointed Mr. Eyal Henkin as the Company's CEO, beginning January 1, 2018.

In August 2018, Ms. Rachel Mittelman was appointed as the Group's Chief Information Officer, commencing in September 2018.

In February 2019, Mr. Assaf Aviv was appointed as the Group's VP Innovation and Business Development, commencing in March 2019.

For further details on the senior officers in the corporation, see a specification with respect to Section 26 and Section 26A in Chapter D of the Report.

## 17.4. Investment in training, instruction and development of human capital

The Group companies hold training and instruction workshops from time to time for their employees in accordance with the employee's position and the Group's needs, in order to ensure that employees have adequate training. Once a year, the Company holds concentrated training for officers and employees of the Company in accordance with the Company's Internal Enforcement Program, including in the areas of securities, planning and building and real estate, labor law, environment, safety and accessibility, prevention of sexual harassment as well as additional training held from time to time according to need. Employees of the Group companies keep abreast of fields touching on their responsibilities in the Group, from time to time, by participating in exhibitions, seminars, conferences and professional courses.

## 17.5. Benefits given to employees and the nature of the employment agreements

Employees of the Group are employed under personal contracts and no collective bargaining agreements apply.

The employment conditions of the Group's employees include, in some cases, *inter alia*, *per diems*, travel expenses/car maintenance/making a vehicle available to the employee, managers insurance/pension fund, advanced training fund, annual leave, recuperation pay, basic health insurance, work disability insurance, payment for global overtime, reimbursement of expenses and a 13th salary.

Additionally, the Group's third-party insurance policy is an extended policy that includes coverage for professional liability for the management companies and the Company's employees who are professionals, with a liability cap of $2 million per incident and per insurance period, as part of the policy's liability cap.

In addition to the above, all of the Company's and the Group Companies' liabilities are covered in respect of the employees' social benefits and termination of the employment relationship by deposits that are made in severance pay funds and insurance policies and/or provisions that exist on the Company's books. For a description of the Company's liabilities in relation to the employees' social benefits and termination of the employment relationship, see Note 20 to the Company's Financial Statements.

## 17.6. Employment of officers and senior management employees of the Group

As of the Report Date, members of senior management in the Group are hired as employees under personal employment agreements or through management agreements.

The Company estimates that the Group headed by the Chairman of the Board, Ms. Danna Azrieli and the CEO of the Group, Mr. Eyal Henkin, as well as the experienced officers and managers in the Company who are considered professional and leading in the field, constitute some of the success factors for the Company's business results.

## 17.7. Company's officers compensation plan

For details regarding the Company's officer compensation policy approved on October 6, 2016 by the general meeting of the Company's shareholders (Ref.: 2016-01-060735), see immediate report of August 28, 2016 (Ref.: 2016-01-111643), which is included herein by way of reference.

# 18. Working capital

## 18.1. Working capital

As of December 31, 2018, the Group has negative working capital (excluding Granite Hacarmel and Azrieli E-Commerce) in the sum of approx. NIS 1.5 billion compared with negative working capital in the sum of approx. NIS 1.3 billion, as of December 31, 2017. The deficit in the working capital derives, *inter alia*, also from the decision of the Company's management, at this stage, to finance its activity through short-term credit, considering the business opportunity of low rates of interest for such credit. For details regarding the Company's board of directors' estimation regarding the deficit in the working capital, see Section 5.2 of the Board of Directors' Report.

The company estimates that should it decide to exchange the said credit for long term credit at any point in time, it would be able to do so and therefore and in view of the reasons listed in Section 5.2 of the Board Report, the aforesaid working capital deficit does not affect its ability to timely repay its liabilities.

For details regarding the Company's liquid means and its credit raising possibilities, see Section 5.2 of the Board of Directors' Report.

## 18.2. Customer credit

In the income-producing property segment there is no customer credit since the lease agreements with tenants contain provisions for payment of rent in advance and for monthly or quarterly periods. The Group collects the rent pursuant to the terms and conditions of the lease agreement, usually, by way of a standing order, bank transfers and postdated checks. The tenants, before the handing over of the leased premises thereto, provide collateral for performance of their undertakings pursuant to the lease agreements and the management agreements (bank guarantees, deposits, promissory notes, personal guarantees, etc.). The cases in which rent is not paid in advance are immaterial to the Group.

## 18.3. Suppliers credit

The Company receives credit from its suppliers (primarily contractors and maintenance service providers) for average periods ranging from 15 to 60 days, after the requested service has been completed (on average - a period of approx. 45 days). The scope of credit from suppliers in the Group, as of December 31, 2018, amounted to approx. NIS 253 million, compared with a sum of approx. NIS 218 million on December 31, 2017.

## 18.4. Working capital of the Granite Segment

As of the Report Date, the Granite Segment (Supergas and GES), has (net) working capital in the amount of approx. NIS 126 million, which includes the total current assets (which mainly consist of cash and short-term deposits, trade receivables, other receivables and inventory) less the current liabilities (which mainly consist of current liabilities to banks, current bond maturities and trade and other payables). Working capital does not include balances of the Granite Group vis-à-vis the parent company, Granite Hashalom.

# 19. Financing

## 19.1. General

Unless otherwise noted, the specification in Sections 19.1-19.16 of this Chapter A does not include reference to financing aspects related to Granite Hacarmel and other companies controlled thereby. For details regarding Granite Hacarmel's financing, see Section 19.17 of this Chapter A. In this section, the term "Group" does not include Granite Hacarmel and other operations of Granite Hacarmel.

The Group finances its activities from independent resources, from bank credit from financial institutions and non-bank credit, including through the issue of bonds from institutional bodies. The Group has liabilities to banking corporations and non-bank financing sources amounting, as of December 31, 2018, to the sum of approx. NIS 9.6 billion (including current maturities). Most of the agreements include provisions pursuant to which the Company has the right to prepayment which is contingent, in most cases, upon the payment of a prepayment fine to the financing entity. Additionally, the loan agreements with banking corporations contain certain conditions, upon the occurrence of which, the banks may accelerate the loan amounts (primarily in the case of restructuring and a change of control in the Company, delinquent payments, receivership, and an adverse change in the value of the collateral, if and insofar as collateral was provided). To the best of the Company's knowledge, as of the Report Release Date, the conditions for acceleration of the loans have not been fulfilled. For details concerning the financial liabilities of the Group as of December 31, 2018, see Sections 5.5 and 5.6 of the Board of Directors' Report. For details concerning projected payments per year, see immediate report on the Company’s status of liabilities dated March 20, 2019 which is published concurrently with this Report. For further details concerning the Company’s financing in general, see Section 5 of the Board of Directors' Report.

## 19.2. The Group’s loan balance (not intended for specific uses) as of December 31, 2018

Set forth below is a specification of the average interest rate and the effective interest rate (which, as specified below, as of the Report Date, is identical to the average interest) on long-term loans and short-term loans that were in effect during 2018, and which are not intended for specific uses by the Group, while distinguishing between bank credit sources and non-bank credit sources:

| As of December 31, 2018 | | | | | | |
|---|---|---|---|---|---|---|
| | Long-Term Loans | | | Short-Term Loans | | |
| | Amount (NIS in millions) | Average Interest Rate | Effective Interest Rate | Amount (NIS in millions) | Average Interest Rate | Effective Interest Rate |
| Non-bank sources – Index-linked financing | 7,204 | 1.28% | 1.29% | - | - | - |
| Banking sources - Index-linked Financing | - | - | - | - | - | - |
| Non-bank sources - NIS financing | - | - | - | 436 | 0.55% | 0.55% |
| Banking sources – foreign currency financing | - | - | - | 20 | 2.03% | 2.03% |
| Total financial liabilities | 7,204 | 1.28% | 1.29% | 456 | 0.62% | 0.62% |

## 19.3. Reportable credit made available to the Company

Set forth below is a specification of the balances of the material loans that were provided to the Company as of December 31, 2018 (NIS in millions)[40].

| Loan provision date | Loan designation | Type of Loan | | | Amount of loan taken (NIS in millions) | Balance (including current maturities) as of December 31, 2017 (NIS in millions | Type and rate of annual interest | Principal repayment dates | Interest repayment dates | Linkage | Guarantees / collateral | Is the Company compliant with the financial covenants? | Payment due date of long-term loans |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | Banking corporation | Short-term | Long-term | | | | | | | | | |
| August 2013 | Financing of Azrieli Center | Institutional body group | | X | 710 | 267 | 1.16% | Semiannual | Semiannual | CPI | Pledge of the rights of Canit Hashalom in part of the lobby floor, the roof floor and Floors 11-49 of the Round Tower in Azrieli Center in Tel Aviv. Acceleration right for standard causes set forth in the agreement, which include, inter alia – an adverse material change in the status of tenants or the ratio between the loan balance as of the calculation date and the value of the Round Tower (according to an external appraisal revaluation once a year) (LTV), as of the elapse of 2 years from the loan provision date exceeds 70% (the rate decreases to 25% over the loan period). | Yes – for the results of the calculation of compliance with covenants, see Note 19D of the Financial Statements | Until August 2021 |
| May 2016 | Current needs | Institutional body | | X | 550 | 532 | 1.5% | Quarterly, as of July/2018 | Quarterly | CPI | Canit Hashalom placed a first-ranking fixed charge in an unlimited amount on the Azrieli Rishonim Center in Rishon LeZion, including its rights to receive rent from the tenants in the property and its rights under insurance policies in relation thereto. Financial covenants as provided in the indentures of the Company's Series B and Series C bonds, i.e.: net debt to net assets ratio not exceeding 60% and equity not to fall below NIS 5 billion. In addition, the Company has undertaken as of April 1, 2018 to maintain a debt to collateral ratio (LTV) of no more than 80%. Furthermore, restrictions on dividend distributions, such that no distributions will be performed if as a result thereof equity shall fall below NIS 6 billion and the debt to assets ratio shall exceed 50%. An undertaking not to create a floating charge identical in rank and scope (pari passu). | Yes – for the results of the calculation of compliance with covenants, see Note 19B(8) of the Financial Statements | April 2028 |

The Company has other non-material loans from banking corporations whose balance in the books, as of December 31, 2018, is approx. NIS 0.2 billion. These loans bear interest ranging between 4.2% and 5.8% and will be repaid in 2019-2020. In addition, the Company has undertaken vis-à-vis some of the banking corporations not to

[40] In accordance with Legal Position No. 104-15: Reportable Credit Event of October 30, 2011, as updated on March 19, 2017, and the parameters approved by the board of directors for the examination of materiality in the Reporting Procedure as part of the Internal Enforcement Program.

create a floating charge on all of its assets without receipt of their consent, and that in the event of a breach vis-à-vis the banking corporations, they will be entitled to accelerate also other loans that shall have been given to the Company.

As of December 31, 2018, the total long-term credit received from Bank Leumi amounts to the sum of approx. NIS 137 million. As of December 31, 2018, the Group's unmortgaged investment properties total approx. NIS 19.7 billion, as specified in Section 5.8 of the Board of Directors' Report, out of the sum total of the Group's income-producing properties in the sum of approx. NIS 27.5 billion. For details on non-bank credit see in this section below.

## 19.4. Reportable credit made available to the Group's companies

Set forth below is a specification of the balances of the material loans that were provided to the Group companies as of December 31, 2018 (NIS in millions):

| Borrowing Corporation | Loan provision date | Loan designation | Type of Loan | | | Sum of loan taken | Balance as of December 31, 2018 (Company's share) (NIS in millions) | Principal repayment dates | Interest repayment dates | Annual interest rate | Linkage | Guarantees / Pledge | Repayment due date of long-term loans |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | Banking corporation / financial institution | Short-term | Long-term | | | | | | | | |
| Shareholders of the property[41] | February 2014 | Acquisition of Three Galleria | Foreign financial institution A | | X | $130 million | 442 | Monthly | Monthly | 5.998% | U.S.$ | Pledge of the property and all of rights related thereto and deriving therefrom. Guarantee by the Company, forfeitable only in several specific instances defined in the loan agreement. The Company's undertaking to indemnify the financer for its damage in the event of certain breaches of the buyer's undertakings in the loan agreement | By March 2021 |

A number of the Group's Companies have other non-material loans whose balance on the books, as of December 31, 2018, is approx. NIS 1,046 million, approx. NIS 1,019 million of which are linked to foreign currency and bear interest ranging between 3.2% and 5.5%, which shall be repaid in 2019-2033 and there are no financial covenants for these loans. A balance of approx. NIS 27 million constitutes a variable interest loan in Shekels against which there are pledges and financial covenants and it will be due for payment in the years 2019-2022.

[41] The loan was taken by Three Galleria Office Buildings, LLC, 90% of which are indirectly held by the Company. The presented amount of the loan is in respect of 100% of the loan.

## 19.5. Non-bank financing for the Company

### Commercial paper

As of the Report Release Date, the Company has two CP series, a rated series in the amount of approx. NIS 295 million (following the repayment of approx. NIS 96 million over the year's course) and an unrated series in the amount of approx. NIS 182 million (after having paid during the Report Period NIS 50 million and extended the series after the date of the Statement of the Financial Position by NIS 42 million). For details regarding the Company's CP see Note 19A to the Financial Statements. For details with respect to the rating of the Company's CP, see Section 0 of this Chapter A.

### Long-term loans from institutional bodies

The Company has a non-material loan from institutional bodies, whose balance in the books as of December 31, 2018 is approx. NIS 0.2 billion. This loan bears fixed interest at a rate of 0.74%. and will be repaid in 2019-2023. The loan is subject to financial covenants, with which, as of the Report Date, the Company complies.

### The Company's Series B Bonds

During the Report Period, principal and interest payments were made in accordance with the payment schedule thereof. As of the Report Date, the balance of the par value of the Company's Series B Bonds is NIS 1,057 million. In accordance with the terms and conditions thereof, the final maturity date of the Company's Series B Bonds is April 1, 2025. For details regarding the current credit rating of the Series B Bonds, see Section 19.12 of this Chapter A.

### The Company's Series C Bonds

During the Report Period, principal and interest payments were made in accordance with the payment schedule thereof. As of the Report Date, the balance of the par value of the Company's Series B Bonds is NIS 1,066 million. In accordance with the terms and conditions thereof, the final maturity date of the Company's Series B Bonds is April 1, 2025. For details regarding the current credit rating of the Series B Bonds, see Section 19.12 of this Chapter A.

### The Company's Series D Bonds

On March 29, 2017, the Company released a shelf offering report for the issue and listing on TASE of up to NIS 1,090 million par value which were offered through the expansion of the Company's D Bond Series, based on a shelf prospectus. On March 30, 2017, the Company announced that according to the issue results, approx. NIS 984 million par value of Series D Bonds more have been allotted in consideration for approx. NIS 960 million (approx. NIS 955 million net of issue expenses).

On January 31, 2018, the Company released a shelf offering report for the issue and listing on TASE of up to NIS 1,490 million par value which were offered through the expansion of the Company's D Bond Series, based on a shelf prospectus. On February 1, 2018, the Company announced that according to the issue results, approx. NIS 1,367 million par value of Series D Bonds more have been allotted in consideration for approx. NIS 1,409 million (approx. NIS 1,400 million net of issue expenses).

During the Report Period, principal and interest payments were made in accordance with the payment schedule thereof. As of the Report Date, the balance of the par value of the Company's Series D Bonds is NIS 4,363 million. In accordance with the terms and conditions thereof, the final maturity date of the Company's Series D Bonds is July 5, 2030.

For details regarding the current credit rating of Series D Bonds see Section 19.12 of this Chapter A.

### The Company's Series E Bonds

After the Report Period, on January 20, 2019, the Company released a shelf offering report for the issue and listing on TASE of up to NIS 1,335 million par value of a new Series E bond series of the Company, by virtue of a shelf prospectus. On January 22, 2019, the Company announced that according to the issue results, approx. NIS 1,216 million par value of Series E Bonds have been allotted in consideration for approx. NIS 1,216 million (approx. NIS 1,207 million net of issue expenses).

For details regarding the current credit rating of the Series E Bonds, see Section 19.2 of this Chapter A.

### The Company's Series F Bonds

After the Report Period, on January 20, 2019, the Company released a shelf offering report for the issue and listing on TASE of up to NIS 315 million par value of a new Series F bond series of the Company, by virtue of a shelf prospectus. On January 22, 2019, the Company announced that according to the issue results, approx. NIS 263 million par value of Series F Bonds have been allotted in consideration for approx. NIS 260 million (approx. NIS 260 million net of issue expenses).

For details regarding the current credit rating of Series F Bonds, see Section 19.12 of this Chapter A.

For further details on the Company's bonds, see Annex C to the Board of Directors' Report and Note 19B(4) to the Financial Statements.

## 19.6. Non-bank financing for the Group's companies

In the year of the Report and as of the Report Date, other than as specified with respect to non-bank financing of the Company in Section 19.5 of this Chapter A, no use of non-bank financing has been made for companies of the Group.

## 19.7. Inter-company loans

Set forth below is a specification of the balances of loans provided between the Group companies, excluding inter-company debit and credit balances, as of December 31, 2018 (NIS in millions) in amounts exceeding NIS 20 million:

| The Lending Corporation in the Group | The Borrowing Corporation in the Group | Date of Provision of the Loan | Original Loan Amount (NIS in millions) | Last Date For Payment | Annual Interest | Linkage | Balance of Loan Amount As of Dec. 31, 2018 (NIS in millions) |
|---|---|---|---|---|---|---|---|
| Canit Hashalom (1) | Gemel Tesua | January 2009 | 74 | January 2019 | — | — | 74 |
| Canit Hashalom (2) | AG Galleria Office Buildings LP | February 2011 | 99 | February 2021 | Libor+ 7.1% | U.S. $ | (3) 107 |
| Canit Hashalom (4) | Gemel Tesua | January 2017 | 270 | December 2018 | 1.5% | Index | 279 |
| Canit Hashalom (5) | Palace America Senior Housing Company | March 2016 | 41 | March 2021 | - | - | 41 |
| Canit Hashalom (6) | Palace Senior Housing Chain | May 2016 | 55 | May 2021 | - | - | 55 |
| Ahuzat Bayit Ra'anana (7) | Palace Lehavim | March 2017 | 91 | December 2021 | 2.61% | | 92 |
| Ahuzat Bayit Ra'anana (7) | Palace Modi'in | October 2016 | 284 | September 2021 | 2.61% | | 281 |

* For a description of the balances of the loans provided by the Company to the Group companies, see Section 11 of Part D of the Report.

1. Against the loan, Gemel Tesua issued a capital note in the sum of NIS 74 million to Canit Hashalom, bearing neither interest nor linkage, and the date of payment thereof will be no earlier than January 1, 2019. Payment of the capital note is not secured by any collateral and is inferior to other Gemel Tesua undertakings and precedes only the distribution of surplus assets upon dissolution.
2. The loan is in the sum of approx. U.S. $28 million.
3. The loan balance, including unpaid interest as of December 31, 2018, is approx. NIS 199 million.
4. Against the loan, Gemel Tesua issued Canit Hashalom a bond in the sum of NIS 270 million. Insofar as Gemel Tesua fails to repay on the due date the principal, interest and linkage differentials accrued until the due date, the bond will be deemed to have been repaid and reissued on the day following the due date.
5. Against the loan, Palace America Senior Housing Company issued Canit Hashalom capital notes in the aggregate sum of approx. NIS 41 million, which bear no interest and linkage and the due date of which will be no earlier than March 23, 2021. The repayment of the capital notes is not secured by any collateral, is inferior to other liabilities of Palace America Senior Housing Company and only precedes the distribution of surplus assets upon the liquidation thereof.
6. Against the loan, Palace Senior Housing Chain issued Canit Hashalom a capital note in the sum of approx. NIS 55 million, which bears no interest and linkage and the due date of which will be no earlier than May 25, 2021. The repayment of the capital notes is not secured by any collateral, is inferior to other liabilities of Palace Senior Housing Chain and only precedes the distribution of surplus assets upon the liquidation thereof.
7. The loans bear an annual interest according to Section 3I of the Income Tax Ordinance.

## 19.8. Credit restrictions

For a description of the Company's undertakings in connection with the issue of the Series B Bonds, Series C Bonds and Series D Bonds vis-à-vis the bondholders, see Note 19B to the Financial Statements. See Note 19B (4) for a description of the Company's liabilities regarding the issuance of Series E Bonds and Series F Bonds after the date of the Statement of the Financial Position.

## 19.9. Credit facilities

As of the Report Date, the Group has not been provided with any binding credit facilities or non-binding credit facilities.

## 19.10. Bank and non-bank credit received between the date of the Financial Statements as of December 31, 2018 until shortly before the Report Release Date

The Company took no bank and non-bank credit in the period between December 31, 2018 and until shortly before the Report Release Date except for the issuance of Series E Bonds and Series F Bonds as specified in Section 19.5 above.

## 19.11. Loans repaid between the date of the Financial Statements as of December 31, 2018 and shortly before the Report Release Date

No such loans have been repaid, over and above current payments in accordance with the payment schedule of each loan.

## 19.12. Credit rating

On January 24, 2019, Ma'alot ratified the Company's AA+/Stable/ilA-1+ rating.. To inspect the full report by Ma'alot, see the Company's immediate report of January 24, 2019 (Ref.: 2019-01-009423), which is included herein by way of reference.

On December 31, 2018 Midroog ratified the rating of the Company's Series D Bonds with an Aa1.il rating with a stable outlook. On January 20, 2019, Midroog confirmed the rating of new bonds of the Company (Series E-F) with an Aa1.il rating with a stable outlook. For inspection of the full reports of Midroog of December 31, 2018 and January 20, 2019, see the Company's immediate reports of December 31, 2018 and January 20, 2019 (Ref. : 2018-01-129381 and 2019-01-003051 respectively), which are included herein by way of reference.

As of the Report Date, the Company's Series B-C Bonds are rated stable AA+ by Ma'alot, and the Company's CP are rated ilA-1+ by Ma'alot. For further details and details on the rating history of the Company's Series B-C Bonds and the Company's CP, see the Company's immediate report of March 28, 2017 (Ref.: 2017-01-030966) which is included herein by way of reference.

As of the Report Date, the Company's Series D-F Bonds are rated by Midroog with an Aa1.il rating with a stable outlook. For further details and details on the rating history of the Company's Series D-F Bonds, see the Company's immediate reports of December 31, 2018 and January 20, 2019 (Ref.: 2018-01-129381 and 2019-01-003051 respectively), which are included herein by way of reference.

### Rating of private loans taken by the Company

The Company has no other rated loans.

## 19.13. Pledges

For details regarding various pledges which were created by the Company and the Group's companies to secure their obligations, see Note 30A to the Financial Statements.

## 19.14. Guarantees

In the ordinary course of business, at the request of the Company and the Group's companies, bank guarantees are issued by banking corporations in connection with their properties, including guarantees to secure the obligations of the Company and the Group's companies. For information regarding guarantees which the Company has extended, *inter alia* in connection with the financing of the acquisition of properties overseas, see Note 30B to the Financial Statements.

## 19.15. Variable interest credit

The Group has several loans at variable interest credit. Most of the credit was taken in Shekel currency linked to Prime or Bank of Israel interest, and the remainder in foreign currency linked to the LIBOR, plus a margin determined in relation to each loan. The foregoing credit changes in accordance with changes in the LIBOR interest or the Prime or Bank of Israel interest.

Set forth below is a specification of the range of (nominal) interest for the periods of the Report, as well as the interest rate in proximity to the Report Release Date in respect of the loans at variable interest:

| Credit type | Currency | Sum of credit shortly before the Report Release Date (NIS in millions) | Interest rate shortly before the Report Release Date (in %) | Interest range in the reporting periods (in %) | |
|---|---|---|---|---|---|
| | | | | December 31, 2018 | December 31, 2017 |
| Non-bank credit | NIS | 477 | 0.6% | 0.6% | 0.4% |
| Bank credit | NIS | 27 | 2.9% | 2.9% | 2.7% |
| Bank credit | GBP | 20 | 2.0% | 2.0% | 1.88% |

The Company and/or the Group's companies will raise additional funds, according the Company's decision, for the purpose of its business operations, the continued construction of projects under development and investment in new projects.

## 19.16. Regulatory Implications

The instructions of the Supervisor of Banks in Israel include borrower group and "individual borrower" limits that affect the provision of credit beyond certain scopes, relative to the total liability of one group of borrowers and total liabilities of the six largest borrowers of the bank. Azrieli Group, together with Granite Hacarmel, and companies controlled thereby may be considered one "group of borrowers" for this purpose.

In accordance with Section 26 of the Concentration Law as defined below, provisions are to be determined in respect of limitations on credit to be provided by financial entities to a corporation or a business group. A 'business group' is defined in said Section as the "controlling shareholder and the companies controlled thereby", notwithstanding the inclusion of any of such entities in the list of centralistic bodies. In the context of the report of the Committee to Assess Debt Restructuring Proceedings in Israel (the "Andorn Committee") that was released in November 2014, several recommendations were included regarding such matter, including a credit limit of business groups, whose effective credit exceeds 5% of the market business credit, and an imposition of a reporting obligation to the Committee for Reduction of Concentration on companies whose effective credit exceeds 3% of the scope of market business credit. As of the Report Date, such recommendations have yet to receive statutory or binding status and the Company is not aware of other new limitations deriving from the Concentration Law. It should be noted that insofar as is known to the Company's management, as of the Report Date, a borrower limit does not apply to the Azrieli Group and/or Granite Hacarmel.

## 19.17. Financing of Granite Hacarmel Group

### 19.17.1. Financing sources

As of the Report Date, Supergas and GES finance their activity from their own means, from short-term bank credit, from project-designated long-term loans some of which are supported by guarantees of the parent companies and from monies received from the issuance of non-negotiable bonds to institutional investors.

### 19.17.2. Loans and interest rates at Granite Hacarmel Group

Details of the average interest rate and the effective interest rate on long-term and short-term loans, from bank sources and non-bank sources, at Granite Hacarmel, Supergas and GES, as of December 31, 2018 and as of December 31, 2017:

As of December 31, 2018:

| | Long-term | | | Short-term | |
|---|---|---|---|---|---|
| | Amount (NIS in millions) | Average interest rate | Effective interest rate | Amount (NIS in millions) | Average interest rate |
| Non-bank sources – Index linked | 323 | 4.9% | 5.3% | - | - |
| Bank Sources – Index linked | 35 | 3.8% | 3.8% | - | - |
| Bank sources – NIS | - | - | - | 27 | 2.3%-2.9% |
| Total financial liabilities | 358 | | | 27 | 2.3%-2.9% |

As of December 31, 2017:

| | Long-term | | | Short-term | |
|---|---|---|---|---|---|
| | Amount (NIS in millions) | Average interest rate | Effective interest rate | Amount (NIS in millions) | Average interest rate |
| Non-bank sources – Index linked | 351 | 4.9% | .53% | - | - |
| Bank Sources – Index linked | 37 | .38% | 3.8% | - | - |
| Bank sources – NIS | - | - | - | 28 | 2.1%-2.9% |
| Total financial liabilities | 388 | | | 28 | 2.1%-2.9% |

### 19.17.3. Credit Facilities

In the Granite Segment, Supergas and GES have short-term credit facilities which are agreed with the banks in the amount of approx. NIS 170 million, some of which are secured and some are not due to the high credit allocation fees. The used credit balances as of the Report Date amount to approx. NIS 82 million (including use in respect of guarantees). Short-term credit from banks bears an unlinked variable Shekel interest rate, which is a function of the Prime interest rate. The Prime interest rate varies monthly according to the decision of the Bank of Israel.

To secure the bank credit extended to Supergas, a floating charge unlimited in amount and a fixed charge on its uncalled and/or unpaid share capital, its goodwill, securities and pledged documents, were registered in favor of the banks that finance its operations. As part of the floating charge, Supergas has undertaken not to create additional charges without the consent of the banks and subject to conditions as set forth in the bonds. To the best of the Company's knowledge, there is an inter-bank agreement between the charge-holding banks, according to which they hold a pari passu charge on the assets of Supergas. To secure the bank credit extended to GES, a guarantee was provided by Granite. In addition, GES has a long-term loan agreement with one of banks, which is intended to finance the construction of a wastewater treatment plant in the BOT Method. Such loan agreement is backed by revenues from the operation of the plant, which are pledged in favor of the financing bank and are backed by Granite's guarantee.

### 19.17.4. Bonds issued by Supergas

In July 2007, a consolidated company of Supergas, which was established for the purpose of the issue and to which were transferred the domestic gas activity and some of the commercial gas activity for marketing gas in portable gas containers, issued to institutional investors by way of a private placement, bonds with a total par value of approx. NIS 600 million. The bonds are rated Aa1 by Midroog Ltd., are for a period of 18 years and have been paid in quarterly principal installments since 2010. The bonds are linked to the CPI (principal and interest) and bear interest at an annual rate of 4.9%, which is paid once every calendar quarter. As of December 31, 2018, Supergas' liability in respect of the bonds amounts to approx. NIS 323 million.

In June 2014, Supergas completed a proceeding for changing the bonds issued thereby in 2007, which included the bringing forward of certain principal payments (constituting approx. 11.5% of the balance of the bonds), which in accordance with the original terms of the issue were due in the course of the next five years, and the flattening of quarterly principal payments such that they shall be uniform and equal. In this context, Supergas repaid 51,829,380 par value in the total amount of approx. NIS 75 million that includes approx. NIS 12.3 million paid due to the repayment due date being pushed forward. In addition, the company undertook, that in the event that Canit Hashalom Investments shall cease to be a controlling shareholder of Supergas, Granite Hacarmel shall make an offer to the bond holders for the purchase of bonds at a scope of no less than 45 million par value and at a price reflecting the adjusted value of the bonds on such date.

The bonds are secured by a first-ranking floating charge, unlimited in amount, on all of the assets of Supergas' consolidated company. In addition, Supergas charged, in a first-ranking fixed charge, unlimited in amount, all of the consolidated company's shares owned and held thereby, including the rights deriving from such shares. In accordance with the terms and conditions of the bonds, Supergas' consolidated company is required to meet financial covenants. Deviation from the financial covenants will allow the bondholders to demand acceleration or prepayment. As of December 31, 2018, Supergas' consolidated company meets the covenants determined. For further details, see Note 19B (5) to the Financial Statements.

For details regarding limitations, including financial covenants of consolidated companies of Granite Hacarmel, see Notes 9 to the Financial Statements.

## 20. Insurance

The Company's insurance policies for the insurance of property and liability include insurance policies which cover certain risks in the Group's assets, up to the amounts set in such policies. These policies include: all-risks property insurance at reinstatement value, which includes coverage of fire, machinery breakdown, loss of rent and loss of profits from machinery breakdown, terror and war insurance, third party liability insurance, employers' liability insurance, contractor work insurance and crime insurance.

The amounts of the Group's property insurance were determined thereby according to its estimation, and the insurance policies are reviewed periodically by the Company's insurance consultants before the Board of Directors.

For details regarding the insurance coverage applicable to the Company's officers, see Note 35D to the Financial Statements.

## 21. Taxation

For details regarding the taxation applicable to the Company and the Group companies (including the Granite Group), see Note 28 to the Financial Statements.

## 22. Environmental risks and the management thereof

In the framework of its activities in the property segment, (including the development segment and the senior housing segment)the Group is required, *inter alia*, to meet the conditions and requirements of the Planning and Building Law, 5725-1965, including the Planning and Building Regulations (application for a permit, the conditions therein and fees), 5730-1970, the Planning and Building Regulations (Environmental Impact Surveys), 5763-2003 etc., *inter alia*, in the framework of approval of zoning plans, building permits, various licensing proceedings under the planning and building laws and the performance of building and construction work. The Group companies are responsible, by virtue of their owning or leasing land, under certain circumstances, pursuant to law, for compliance with the provisions of the environmental protection laws, including the Water Law, 5719-1959, the Business Licensing Law, 5728-1968 and the Hazardous Substances Law, 5753-1993, the Nuisance Prevention Law, 5721-1961, Sewage and Water Corporations Rules (Plant Wastewater Discharged into the Sewage System), 5771-2011, the Maintenance of Cleanliness Law, 5744-1984, the Senior Housing Law, 5772-2012 and more. A considerable tightening of the aforesaid regulation may have material implications for the Group’s business results and the amount of expenses required consequently thereto. In this context it is noted, that as of the Report Release Date, several bills are pending which, if passed, will affect the Group’s business, including: the Prevention of Soil Pollution and Treatment of Polluted Soil Bill, 5771-2011.

It shall be noted that in recent years, environmental activity, in Israel and worldwide, has significantly increased, as expressed, *inter alia*, in supervision and enforcement by government agencies and activity by environmental organizations. In the Group’s estimation, this trend is expected to continue in the coming years. The Group is investing many resources in ensuring its compliance with the provisions of the environmental laws that apply thereto, and is acting to prevent and minimize the environmental risks from its activity.

The Group’s policy is to comply with the provisions and requirements of the law, including the environmental laws, as well as the requirements of the various supervisory bodies. For this purpose, professional environmental consultants are assigned to each project of the Group, who assist the Group and advise it throughout the project.

Complex at the Check Post Intersection in Haifa - In accordance with the information leaflet that was received from the City of Haifa, the lot that is located at the Check Post intersection in Haifa may be affected by hazardous substances. As of the Report Release Date, the Company has not yet received any additional update from the authorities with respect to such hazardous substances. The Company carries out, in coordination with the Ministry of Environmental Protection, various tests on the soil.

Cellular rental space - In some of the Group's income-producing properties, the Group leases space to the cellular companies (the "Leased Space") for the purpose of installing and operating cellular antennas and/or miniature transmitters (the "Telecommunications Equipment"). In accordance with most of the agreements between the Company and/or the Group's management companies and the cellular companies, responsibility for obtaining all of the approvals required by law to set up and operate the antennas and/or miniature transmitters, and responsibility for complying with the various environmental protection laws lies with the cellular companies, including holding, so long as they lease the Leased Space, the approval of the Radiation Commissioner at the Ministry of Environmental Protection regarding instructions and restrictions relating to the use of the Telecommunication Equipment, and acting in accordance with this approval, and they also undertake to comply with the safety instructions that shall be published by the Company or the management companies. Additionally, in the framework of these agreements, the cellular companies undertake to indemnify and compensate the Company and/or the management companies for any damage and/or expense that shall be caused as a result of the cellular companies' activities on the Leased Space, and for their liability by law for any act or omission of the cellular companies, and they undertake to insure their liability under the law for any damage and/or harm that may be caused to a third party. Finally, pursuant to the provisions of most of the agreements as stated above, each cellular company undertake to cooperate with the other cellular companies with which the Company has engaged, with respect to the operation of the Telecommunications Equipment in the Leased Space.

Water and Sewage Corporations (Plant Wastewater Discharged into the Sewage System) Rules, 5771-2011 – In the Report Period, the Company is acting in relation to several properties owned thereby vis-à-vis the water and sewage corporations at the relevant authorities in order to arrange the issue of the waste water discharged by certain businesses leasing space in such properties, which ostensibly result in deviations in the values of the waste water discharged into the municipal sewage system. The Company has retained professional consultants on the matter and places great importance on strict compliance in environmental issues.

# 23. Restrictions on and Supervision over the Corporation

Below is a brief overview of the laws, regulations, orders, restrictions and requirements with which the Group is obligated to comply in its various operating segments:

## 23.1. In Israel

### 23.1.1. Real estate operations

The Company's operations in Israel is subject to the land laws, including in relation to land taxation and lease and borrowing laws, as well as directives and contracts of the Israel Land Authority and Local Authorities, planning and building laws and environmental laws.

### 23.1.2. General laws concerning the Group's operating segments

In the framework of its activities, the Company and the Group companies are subject to municipal bylaws in each one of the local authorities in which the Group's income-producing properties are located, insofar as relevant, including regarding the opening and closing of businesses, the Prevention of Smoking and Exposure to Smoking in Public Places Law, 5743-1983, Equal Rights for Persons with Disabilities Regulations (Service Accessibility Adjustments), 5773-2013, Water and Sewage Corporations rules, the Privacy Protection Law, 5741-1981, the Communications Law (Telecommunications and Broadcasting), 5742-1982 ( which includes clauses addressing "Spam") etc.

Furthermore, some of the Group's companies purchase electricity through a high-voltage connection and supply the electricity to tenants according to a low-voltage tariff as determined and updated from time to time by the Electricity Authority (PUA-E). To the best of the Company's knowledge, as of the date of the Report, the Ministry of Energy and the PUA-E are acting for the regulation of electricity distribution in retail centers and malls across the country.

### The Concentration Law

December 2013 saw the publication of the Promotion of Competition and Reduction of Concentration Law, 5774-2013 (the "Concentration Law"), which implements the main recommendations of the Committee for Increasing Competitiveness in the Economy. The law includes three main chapters, as follows: (a) limitation of control in companies in a pyramid structure; (b) separation between significant non-financial corporations and significant financial bodies; (c) weighing of economy-wide concentration considerations and sector-specific competition considerations in the allocation of rights by the State. The last two chapters may be relevant to the Company, if no change occurs in the scope of its business and holdings, as being as of the Report Date.

Creation of separation between significant financial bodies and significant non-financial bodies (as such terms are defined in the Concentration Law). The main restrictions set forth in the Concentration Law in respect of the separation of significant financial bodies and significant non-financial bodies are, *inter alia*: (1) generally, a significant non-financial corporation or the entity controlling it shall not control a significant financial body and shall not hold more than 10% of a certain type of means of control in a significant financial body, and shall not hold more than 5% of a certain type of means of control in a significant financial body which has no controlling shareholder; and (2) no person holding more than 5% of a certain type of means of control in a significant non-financial corporation shall control a significant financial body; all subject to the conditions, exceptions and restrictions as were determined in the provisions of the Concentration Law. The aforesaid notwithstanding, a significant non-financial corporation which, on the eve of publication of the Concentration Law, duly held means of control in a significant financial corporation, at a rate exceeding the holding rates specified above, may hold such means of control for 6 years from the date of publication of the Concentration Law (i.e. until December 11, 2019), subject to the conditions set forth in the Concentration Law. The Concentration Law prescribes that the Committee for the Reduction of Concentration shall release the list of the centralistic entities. This list includes the list of corporations included in the definition of a significant non-financial corporation[42] and the list of the entities included in the definition of a significant financial body. On December 11, 2014, the centralization committee released the list of centralistic entities in the market on the Ministry of Finance's website.[43]

According to the list, Azrieli Group was included in the list of the significant non-financial corporations. In April 2015, the Competition Commissioner published an updated list of the significant financial bodies according to the Concentration Law and included Leumi Card (which was not included in the original list) therein. Accordingly, the Group was required to reduce its holdings in the shares of Leumi Card below a 10% holding rate by December 11, 2019. On February 25, 2019, the Company closed the sale of all of its holdings in Leumi Card. For details regarding the closing of a transaction for the sale of all of the holdings of the Company and Bank Leumi Le-Israel Ltd. in Leumi Card to a corporation controlled by the Warburg Pincus Foundation, see Section 1.3.9 of Chapter A above.

It is noted that, from time to time, the Concentration Committee publishes in the Official Gazette updates to the lists of significant non-financial corporations, significant financial bodies and centralistic entities. In the last update of such lists, published on December 9, 2018, Azrieli Group (and the controlling shareholders thereof and the corporations controlled by them) and Granite Hacarmel Group are listed among the significant non-financial corporations.

### Privacy Protection Regulations (Information Security), 5777-2017

On May 8, 2017, the Privacy Protection Regulations (Information Security), 5777-2017 were approved by the Constitution, Law and Justice Committee. The purpose of the Regulations is, *inter alia*, to define information security principles related to the management and use of information in databases, based on information security standards that are generally accepted around the world, all with the purpose of providing protection for the rights of the subjects of the information in the database from abuse of the information about them. The Regulations prescribe several provisions in relation to the definition and periodic update of risks, the setting of information security procedures according to the database's sensitivity, and also address the physical aspects of safeguarding the database and the need to secure it.

### 23.1.3. Senior housing

Restrictions on and supervision of the senior housing operating segment

Operations in the senior housing segment are mostly regulated by the provisions of the Senior Housing Law, which prescribes, *inter alia*, the duty to receive an operation license for the management and operation of a senior home, provisions in respect of the requirements and conditions for the receipt of a senior home operation license, the contractual relationship between the operator and the tenant, the duty to enter into a written engagement agreement, the provision of collateral to secure the repayment of the funds of the tenants' deposits, provisions in connection with vacation of tenants, and more.

Below are additional provisions of law applicable to the senior housing segment, as prescribed by the Senior Housing Regulations which took effect during December 2017 and January 2018, as specified in this Chapter A:

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[42] The definition of a significant non-financial corporation principally includes an effective sales turnover exceeding approx. NIS 6 billion or effective credit exceeding approx. NIS 6 billion. For the accurate definitions, the binding language of the Concentration Law must be consulted.

[43] The address of the Ministry of Finance's website: http://mof.gov.il/Committees/Pages/CentralizationDecreaseCommittee.aspx

The Senior Housing Law

The Senior Housing Law prescribes, *inter alia*, that the operation of senior homes requires the receipt of an operation license on behalf of the Commissioner of Senior Homes at the Ministry of Social Affairs and Social Services (the "Commissioner of Senior Homes") and compliance with several conditions prescribed by the said law, including the applicant for the license being the owner or long-term leaseholder of the land of the senior home in respect of which the license is requested, there being no conviction of the license applicant and the senior home manager of certain offences, proof of the financial stability of the license applicant to ensure the proper operation of the senior home and so forth. The operation of a senior home without an operation license or other than according to the conditions of the license constitutes an offence that carries various fines and incarceration penalties. As of the Report Release Date, the regulations regulating the issuance of the operation licenses for senior homes have not yet been published.

Furthermore, the Senior Housing Law regulates additional matters, including the following: (1) The duty to make a written engagement agreement between the holder of the senior home operation license (the "Operator") and the person seeking to be a tenant of the senior home; (2) The specification of basic mandatory services the Operator is obligated to provide the tenants; (3) The duty to set up an LTC unit for senior homes consisting of at least 250 residential units, while the Commissioner of Senior Homes is authorized to exempt the senior homes from this duty in accordance with the terms and conditions stated in the Senior Housing Law[44]; (4) Limitation on arbitrary increases of the management fees and any other payment, which the tenant does not have the actual ability to waive; (5) The right of the tenants to set up a tenants' representative body at the senior home, and more.

In addition, the Senior Housing Law prescribes that in any case in which the tenant is required to deposit sums on account of the Deposit[45], which exceed a rate of 7% of the sum of the deposit or NIS 70,000, whichever is lower, the Operator will be required to provide the tenant collateral to secure the funds of the Deposit, according to the Operator's choice and pursuant to the following alternatives: (1) Bank guarantee; (2) Insurance of the tenant with an insurer and specification of the tenant as an irrevocable beneficiary in the insurance contract, provided that the insurance fees are paid in advance; (3) Transfer of 40% of the amount of the Deposit to a trustee under a trusteeship contract in which the tenant is specified as a beneficiary; or (4) Registration of a first-ranking mortgage on the real property in favor of the tenant. It is noted that the tenant may waive the receipt of such collateral, provided that the waiver is given in writing. Furthermore, the Operator is obligated to bear 20% of the cost of provision of the collateral, with the balance of the cost, at the rate of 80% as aforesaid, being borne by the tenant. The Senior Housing Law lists causes for enforcement of the collateral by the tenant, including the insolvency of the Operator, an order for stay of proceedings, an order for receipt of assets, a liquidation order, an order for appointment of a receiver, or circumstances wherein an absolute impediment to the repayment of the funds of the deposit is created.

Amendment of the Senior Housing Law

On July 25, 2018, an amendment was published to the Senior Housing Law (the Senior Housing Law (Amendment), 5778-2018) (the "Amendment to the Law"), which concerns the amendment of the provisions pertaining to the collateral used to secure the funds of the residents' deposits. The principal amendments to the Senior Housing Law are as follows: (1) Imposition of a duty on the operator to provide collateral to secure the full amount of the deposit deposited by the resident (i.e. "from the first Shekel"), such that the operator may not receive from a resident a sum exceeding 7% of the deposit or NIS 70,000, whichever is lower, other than subject to the registration of a first-ranking mortgage in favor of the resident or the depositor, on the operator's right in the land on which is built the senior home in which the resident resides (barring parts of the land that serve as retail space

[44] It is noted that the provisions of the Senior Housing Law concerning the setting up of an LTC unit took effect at the lapse of five years as of the date on which the law took effect, i.e., on December 3, 2017.

[45] "Deposit" – A payment made by a tenant to an operation license holder under an engagement agreement, including as collateral for compliance with the terms and conditions of the engagement agreement, which, under the terms and conditions of the engagement agreement the operation license holder must repay the tenant, in whole or in part, when the engagement comes to an end, after deduction of any sum deducted from such payment under the provisions of the engagement agreement and the law.

or as part of the senior home's LTC unit), which mortgage shall be registered in the name of a trustee who shall be appointed by the residents (according to the proportionate share of each one of them in the sum of the deposits) or, if the senior home is registered as a condominium, in the name of the resident or the maker of the deposit, or alternatively, subject to the provision of a bank guarantee or the deposit of 40% of the deposit with a trustee, with the resident as the beneficiary; (2) The operator will bear all of the costs involved in the provision of the aforesaid collateral (as distinguished from the duty to bear 20% of such costs under the provisions of the Senior Housing Law prior to the date on which the Amendment to the Law takes effect, as specified above); (3) Denial of a resident's right to waive such collateral, such that the provision of collateral will be mandatory; (4) Determination of collateral of the type of a cautionary caveat as an undertaking to register a mortgage as temporary collateral, for a period of up to two years, in favor of a trustee to be appointed by the residents, or in favor of the resident, or, if a condominium has been registered, in the name of the resident or the depositor.

Furthermore, pursuant to the provisions of the Amendment to the Law, an irregularities committee shall be established at the Ministry of Welfare, which may exempt an operator, at its request, fully or partially, from provision of the collateral under the Senior Housing Law, and determine conditions to such an exemption, or alternatively, order the provision of alternative collateral.

The Amendment to the Law further stipulates that the Commissioner of Senior Homes may require the operator, at any time, to prove its financial stability by conducting such inspections as determined in the Law and also deliver the results of such inspections to the residents, subject to the conditions specified in the Amendment to the Law.

In addition, provisions were determined regarding the establishment of a joint fund for the financing of medical expenses under circumstances of insolvency for the benefit of all of the residents, and the establishment of a joint fund for the financing of expenses due to insolvency – these funds will be managed by the Custodian General.

The Amendment to the Law includes transitional provisions whereby the provisions of the law shall apply retroactively, such that they will also apply to agreements that were made prior to the amendment. The Amendment to the Law will take effect 18 months after the publication thereof (i.e. in late January 2020), with the exception of the sections concerning the irregularities committee, the examination of financial stability, the fund for the financing of medical expenses under circumstances of insolvency and the fund for the financing of expenses in a case of insolvency, which took effect 6 months after the date of publication (i.e. at the end of January 2019).

In the Company's estimation, the Amendment to the Law does not materially affect the Company or its profits.

The Senior Housing Regulations

<u>The Senior Housing Regulations (Disclosure Document Form), 5778-2018 –</u> These regulations took effect on April 5, 2018 and determine the content of the disclosure document that the operator is required to hand over to a resident with whom the operator expects to enter into an engagement agreement. According to these regulations, the operator is required to disclose and provide to the prospective resident, *inter alia*, information and details regarding the operator and its identity, details about the operator's license, details about services to be provided by the operator, details regarding the operator's rights in the land on which the senior home is built and operates, a description of the public areas, a breakdown of payments, a specification of collateral, and all other details required to be disclosed in accordance with these regulations and the Senior Housing Law.

<u>Draft Senior Housing Regulations (Examination of Financial Stability), 5778-2018 –</u> These regulations were published for public comments on March 27, 2018. These regulations determine the financial conditions required of a license applicant, *inter alia*, to prove its financial stability, and as a condition to receipt of an operating license. In accordance with the provisions of these regulations, the license applicant is required to deliver to the Commissioner of Senior Homes, *inter alia*, financial statements and other documents certified by a CPA on its behalf. The regulations also set forth the tests for examination of the license applicant's compliance with the

regulations, as well as an appeal mechanism. To the best of Palace management's knowledge, the period for submission of the public's comments ended on April 17, 2018, although they have not yet been presented for discussion at the Knesset's legislative committees, and considering that the language is merely preliminary (and subject, *inter alia*, to public comment), the language of the said regulations, if approved, may be different to that presented for public comment.

Senior Housing Regulations (Apartment Specifications Form), 5778-2017 – These regulations took effect on January 17, 2018. In summary, these regulations obligate the Operator to attach to every engagement agreement with tenants (pertaining to the occupancy of an apartment in a senior home) a detailed and accurate specification, which addresses all of the details and information as specified in the said Regulations. Furthermore, the Regulations stipulate that in respect of contracts between senior homes and tenants regarding the occupancy of senior homes in planning stages or under construction, which construction is yet unfinished, a plan of the future apartment, including exact measurements, must be annexed to such contracts in addition to the specifications form of the future apartment;

Senior Housing Regulations (Tenants' Committee), 5778-2017 – These regulations took effect on December 3, 2017. In summary, these regulations pertain to the right of tenants in senior homes to appoint a representative body on their behalf, and prescribe procedures for the selection of such representative body, its powers, the manner to convene its meetings, its voting manner, its term of office and so forth.

Senior Housing Regulations (Provisions regarding Experience, Professional Training and Seniority of Senior Homes Managers), 5778-2017 – These regulations took effect on December 14, 2017. These regulations set forth the preliminary conditions and the experience and professional training requirements of a manager of a senior home, which include, *inter alia*, a duty imposed on a senior home manager to participate in a course and training according to various criteria prescribed by the Regulations, as well as a requirement of having at least three years' experience. Furthermore, these regulations obligate the owners of senior homes to ensure the enforcement and the implementation of these Regulations. The Regulations further anchor the prohibition on senior home managers to act in conflict of interests in the context of their position.

With the exclusion of the above specified regulations, as of the Report Date, additional regulations applicable to the senior housing segment did not yet take effect. To the Company's best knowledge, at this point there are additional regulations which pertain to the senior housing segment and which legislation is yet incomplete, as follows: Draft Senior Housing Regulations (Application for a Senior Home Operation License), which specify the conditions and the documents required for submitting an application for the grant or renewal of a senior home operation license.

Invalids and the mentally frail– The People's Health Ordinance and Regulations

The People's Health Ordinance, 1940, the People's Health Regulations (Registration of Hospitals), 5726-1966, and the People's Health Regulations (Nursing Staff in Clinics), 5741-1981, prescribe that the operation of hospitals, including units for invalids and the mentally frail, requires receipt of a permit from the Ministry of Health and is subject to supervision thereby. Such regulations include provisions with respect to the physical structure, the condition of the equipment, the manner of management, the rights of hospitalized patients and manpower capacities and training.

Labor law

Palace has employees in the senior housing operations and has also engaged with manpower agencies and manpower contractors for the receipt of various services in the senior homes, including cleaning, protection and security. Palace is therefore subject to the labor law and particularly to the law applicable to engagement of contractor employees, including the Employment of Workers by Manpower Contractors Law, 5756-1966, the regulations promulgated thereunder, and the Enhancement of Labor Law Enforcement Law, 5772-2011.

Planning and building laws, work safety and accessibility and consumer legislation

In the context of the planning, development and construction processes of senior homes, Palace is subject, *inter alia*, to the planning and building laws, including the decisions of local authorities and the various zoning committees, and is also subject to the Equal Rights for Persons with Disabilities Law, 5758-1998 and the secondary legislation thereunder, and to the work safety laws. Furthermore, the operation of senior homes is subject to consumer laws, such as: the Consumer Protection Law, 5741-1981 and the Control of Products and Services Law, 5718-1957.

#### 23.1.4. Business Licensing

In the framework of the operations of the Group's companies, some of the Group's companies are required to obtain a business license pursuant to the Business Licensing Law, 5728-1968. To the best of the Company's knowledge, as of the Report Date, all of the Company's properties have a valid business license or are in the midst of proceedings for the renewal or issuance of a business license (including such which had expired), as required under the Business Licensing Law, 5728-1968. In addition, in the lease agreements in which the Group engages with the various lessees, the lessee is required to hold a business license as required by law for the operation of its business in the property.

#### 23.1.5. Economic Competition

In the framework of expansion of the Group's operations, *inter alia*, by acquiring shares in companies owning the rights in real properties, by the Group and the Group's companies may require, under certain circumstances, to approve the merger pursuant to the Economic Competition Law, 5748-1988.

For details regarding restrictions and supervision in the Granite Segment, see Sections 12.2.2 and 12.15 of Chapter A of the Report.

### 23.2. Outside Israel

The Group's operations in the U.S. and in England are subject to the laws and regulations in the said countries and *inter alia* in the field of land, planning and building and lease, the environment and laws on the municipal level and in connection with land taxation.

## 24. Material Agreements and Collaboration Agreements

The Group is a party to collaboration agreements with third parties with respect to some of the projects within the Group's activities.

Excluding agreements which were specified in this Chapter, in the Additional Details Chapter (Chapter D of the Report) and in the Notes to the Financial Statements, the Company is not a part of any material agreements which are not in the ordinary course of business or which were not described in Chapter A of the Report.

## 25. Legal Proceedings

As of the Report Date, the Company and/or the Group companies are not a party to pending material legal proceedings, except as specified in this Report and in Note 32 to the Financial Statements. In addition, as of the date of this Report, the Company and/or the Group companies are conducting various proceedings, as determined by law, *inter alia*, for the resolution of demands received from the various local authorities in respect of mandatory payments and levies, in a total amount that is immaterial to the Company. In respect of part of the proceedings, the Company included provisions in the Financial Statements on the basis of the opinion of the Company's outside advisors, under the circumstances of each matter.

## 26. Goals and Business Strategy

As a leading company in its segments of activity, the Company focuses on the income-producing real estate sector, mainly in Israel. In the mall and retail center segment, the Company regularly focuses, on improving its existing properties, and acts to optimize the utilization of its commercial space and create a suitable tenant mix according to the changing demand needs, increase the number of visitors while maintaining and even improving the attractiveness of its malls and retail centers, increasing the tenants' revenues, and continuing to offer management services to its properties through the Group’s management teams, maintaining the level of its tenants and renewing the lease agreements therewith for additional long-term periods. In the office segment, the Group laid an emphasis on the location of the property, the uniqueness of the building, accessibility and parking, and supporting functions for the tenants and their employees in order to create differentiation against competing properties in the same areas of demand. In the senior housing segment, the Group laid an emphasis on the location, standard of service, varied activities’ contents and a supportive environment.

The Group’s business strategy is mainly to continue to invest in expanding its widespread activity in retail centers and malls (including power centers), the office and other space for lease in Israel and overseas and later on the development and expansion of the senior housing segment and fields which are related to the Company’s business segments, through the purchase of lands for development and construction of assets and/or the purchase of additional assets. In addition, the Company emphasizes the betterment of existing assets, the advancement of building plans and expansions for optimal use of the rights in its assets. The Company insists on maintaining its high financial soundness and a relatively low level of leverage.

One of the Company's goals is investment of not more than approx. 15% of the value of the Company's investment property in Western countries (mainly the U.S.) with a high investment rating, subject to the right timing and appropriate cost.

The Company estimates that its main growth engines are, *inter alia*, the projects undergoing planning and construction, development and construction of new assets through the identification of lands for purchase while taking into account areas of demand, large population centers, central transportation junctions and high accessibility to public transportation.

Furthermore, the Company examines from time to time additional options to expand its segments of activity in other fields of business which are synergetic or tangential to the Company’s business as additional growth engines, while taking advantage of market conditions and/or crisis conditions in leading, cash generating target companies. In the Report Period, the Company continued to develop the senior housing operations, and opened the senior home in Modi’in. In addition, the Company operates the longstanding senior home "Palace Tel Aviv", which it purchased in 2015, and the senior home “Palace Ra’anana” (formerly Ahuzat Bayit Ra’anana), which was purchased in 2016, the Company is continuing to build the senior home in Lehavim and is acting to promote the construction of additional senior homes, as specified in this Chapter A above. The Company aspires to continue developing the senior housing business and to create a significant portfolio with national presence and a 4-5 star finishing standard. In the Report Period, the Company continued to examine various ventures for the construction of new senior homes, identification of suitable land and purchase of existing senior homes, aiming to be a leading player in the senior housing market, both in terms of the number of residential units offered to tenants and in terms of the standard of the provided services.

As reported thereby, the Company regularly reviews the holdings which are not at the core of its business in the real estate sector. For details on a transaction that was closed for the sale of Sonol, see Section 13 of this Chapter A.

The Company's goals as of the Report Release Date are based on the management's estimates in connection with the market conditions as of such date, and there is no certainty that the aforesaid will indeed materialize. For further details, see the Board of Directors' Report.

## 27. Forecast for Development

As the Company reported in the past, during the Report Period until the Report Release Date, the Group has continued exploring business opportunities, in Israel and overseas, in connection with the expansion of its business, mainly in the real estate sector, including continued development of the senior housing segment and entry into related and other operating segments. These opportunities are examined both through the purchase of land reserves and the development of properties, and by way of purchase of properties and/or operations from third parties and/or the betterment of the existing properties owned by the Group, some of which have materialized as stated in the Company's reports. The Company is regularly engaged in identifying opportunities for expanding retail and office space in its existing properties as an addition to existing projects and is pursuing the promotion of the betterment of such properties and is expected to continue pursuing such activity also in 2019. In addition, following the sale of Sonol, the Company continues to regularly look into the other holdings which are not in its core business of income-producing real estate, including the sale of its holdings in Granite Hacarmel (as a whole or its various parts) and/or its financial holdings, all according to its discretion as to the timing, structure and consideration of the transaction. As of the Report Date, there are no short-term plans which deviate from the Company's ordinary course of business and which may have a material influence on the Company's business and results.

## 28. Discussion of Risk Factors

In the Company's estimation, the Group is exposed to several fundamental risk factors deriving from the economic environment and the Group's unique characteristics.

The information concerning risk factors to which the Group is exposed is forward-looking information as defined in the Securities Law. The Company's expectations with respect to this issue are based on past experience, the Group's familiarity with the markets in which it is active and its estimations in relation to its economic and business development. However, the Group's estimations regarding the following risk factors, including the scope of their effect on the Group's business, is forward-looking information as defined in the Securities Law, which is based on the Group's existing information as of the Report Date and it further includes estimations and analysis of the Group. The effect of the realization of any particular risk factor may vary from the Group's estimations, *inter alia* due to external factors that may be beyond the Group's control. Furthermore, in view of the Group's continued examination of the expansion of its business, in particular in the real estate segment, the Group may by exposed in the future to additional risk factors, and the effect of any risk factor, if realized, may vary from the Group's estimations. Notwithstanding the aforesaid, it is noted that the Group's operations are characterized by a large number of tenants, numerous segments and geographic dispersal. These characteristics allow the Group to reduce its exposure to changes in a specific operating segment and to reduce its exposure to the business of a specific tenant.

### 28.1. Macro-economic and financial risks

#### 28.1.1. The growth and consumption rates in Israel

The Company's activity is dependent, *inter alia*, on the growth of the Israeli economy and the per capita consumption rates, which affect the demand for the Company's income-producing properties and the soundness of material tenants of the Group's properties and their ability to fulfill their undertakings thereto.

### 28.1.2. A change in the building inputs index

An increase in the building inputs may affect the price of the Company's engagement with sub-contractors. While construction costs are usually linked to the building inputs index, income is usually linked to the consumer price index. Therefore, the Company may be exposed to negative effects in the event of changes in these indexes.

### 28.1.3. Changes in the economy’s interest rates

A majority of the Group’s undertakings and Group’s development plans are affected by changes in the economy’s interest rates and the banking corporations' conditions for provision of bank credit. A long-term increase in the market interest rates may affect the Group’s financing costs in relation to each project, the yield from the properties, the value of the income-producing properties and the Group’s profitability.

### 28.1.4. Security situation

Changes in and aggravation of the security and political situation may affect the Company’s activity and business results, both from the perspective of the public’s readiness to visits the Group’s shopping centers and malls, in high-stress areas and in general, as well as from the perspective of demand for lease spaces, shortage in manpower in the construction industry, building cost appreciation, etc.

### 28.1.5. Regulatory changes in the Company's business environment

The Group's activity is exposed to various regulatory limitations, including in accordance with the antitrust law, the securities law, corporate law and the supervision on banks law. Stricter regulation in areas pertaining to the Company, as well as possible implications of further regulatory changes might reduce and/or limit the Company's activity through, *inter alia*, organizational changes and the imposition of conditions on the Company's business activity and financial holdings.

### 28.1.6. Changes in the value of financial investments available for sale

In view of the condition of the capital market in Israel, the Company is exposed, to a certain extent, to adverse changes in the value of the companies in which it has invested as a financial asset available for sale. Impairment of these companies may adversely affect the comprehensive income of the Company and its equity.

## 28.2. Industry-specific risks

### 28.2.1. A decline in the demand for rental space

A decline in the demand for rental space and/or renewal of existing lease agreements may lead to a decline in occupancy rates in the Group’s properties and a decline in income from rent and in asset value and will necessarily harm the Company’s business results.

### 28.2.2. A decline in the rent prices

A decline in the demand for rental space together with competition becoming fiercer in the industry may lead to erosion of the Company’s rent, a decline in asset value, and harm its financial results.

### 28.2.3. Strength of main tenants

Damage to the financial strength of tenants, and particularly main tenants, may lead to an increase in provisions for doubtful debts or alternatively, termination of lease agreements and/or eviction of tenants from the Group's properties, and therefore to a decrease in the Group's income from rent and necessarily harm the Company's business results.

### 28.2.4. Competition

The income-producing commercial property segment in Israel is subject to significant competition. For details regarding the effect of the Group's competitors on its business results, see Sections 8.4 and 9.2 of Chapter A of the Report.

### 28.2.5. Approvals from the authorities

Activity in the income-producing property segment is characterized by the need to obtain permits from various entities at the different authorities, particularly in the area of usage and rights confirmations (zoning plans), obtaining building permits, business licenses etc. A delay in obtaining any permit or failure to obtain a permit could harm the profitability of the project or entail various financial expenses for the purpose of compliance with the requirements of the authorities for receipt of the approvals.

### 28.2.6. Legal and regulatory requirements, including with respect to environmental protection

The Group's companies are subject to legal and regulatory requirements from various aspects and, *inter alia* on issues pertaining to the environment (nuisance, underground and above ground pollution, toxic waste etc.), and they are required to bear the costs involved in meeting the same, such that it may have an adverse effect on their results. A toughening of such regulatory requirements may force the Group to allocate additional financial resources to this issue.

### 28.2.7. Changes in the tax burden

The Group's companies are subject to the tax laws in the jurisdictions in which they operate. Changes in the present or future tax rates, or other changes in tax laws that affect the tax liability of the companies, will cause a change in the Company's financial results.

### 28.2.8. Cyber Risks

Within their operations, the Group's companies use computing systems and/or computer-based systems and infrastructures (in this Section below: the "Systems"), including for the sake of information collection and processing on databases managed thereby. A cyber attack intended to penetrate or damage the Systems, the proper use of the Systems, or the material stored thereon, could cause direct and indirect damage, including the disruption, interference or shutdown of operations, ransom attacks, leakage and loss of information, theft of an asset, intelligence collection, damage to goodwill and/or public trust and recovery expenses. The Group operates to prevent and reduce the exposure to the said risks, *inter alia* through protection systems and software, integration and enhancement of information security culture in the Group (including training for managers and employees), clarification and adaptation of procedures, internal control plans as well as monitoring and support with the assistance of experts in the field.

## 28.3. Company-specific risks

### 28.3.1. Fluctuations in the Consumer Price Index

The Group has loans and bonds and deposits from senior housing residents that are linked to the Consumer Price Index and therefore the Group is exposed to fluctuations in the Consumer Price Index. However, most of the Group's revenues from rent in the commercial centers and malls segment and the office and other rental space segment are linked to the Consumer Price Index, while a rise in the Consumer Price Index may lead to an increase in the revenue from rent and reduce the exposure in relation to this risk.

### 28.3.2. Foreign Currency Risks

The Company has assets and liabilities that are stated in various foreign currencies. In view of the fact that the total foreign currency liabilities are not always equal in value to the total foreign currency assets, the Company is exposed to possible changes in the exchange rate of the foreign currencies versus the NIS. However, the Group's revenues from rent in the income-producing property in the USA segment are stated in foreign currency, while a rise in the exchange rate of the foreign currency may lead to growth in revenues from rent and to reduction of the exposure due to this risk.

### 28.3.3. Dependency on Financing Sources

The Company's activity is also financed by external sources and an adverse change in the conditions for provision of credit and/or renewal of existing credit may materially harm the Company's results.

### 28.3.4. Debt raising costs

Changes in the market interest rates may affect the cost of debt raising by the Company as well as the financing expenses.

## 28.4. Senior-housing specific risks:

### Regulation in the senior housing business

The senior housing sector has developed significantly in recent years, along with the regulation of the sector. For details regarding the Senior Housing Law which provides, *inter alia*, the conditions for receipt of a senior home operation license, including the amendment to the Senior Housing Law, see Section 23.1.3 of this Chapter A.

Set forth below are the main risk factors described above that were ranked, in accordance with the Company's estimate, according to the extent of the effect that they may have on the Company's business:

| | The Extent of the Effect of the Risk Factor on the Company | | |
|---|---|---|---|
| | Large Effect | Medium Effect | Small Effect |
| Macro-Economic Risks | | | |
| Growth and consumption rates in Israel | X | | |
| The security condition in Israel | X | | |
| Changes in the interest rates in the economy | | X | |
| Changes in the Building Input Index | | | X |
| Regulatory changes | | X | |
| Changes in the value of available for sale financial investments | | | X |
| Industry-Specific Risks | | | |
| Decline in the demand for rental space | X | | |
| Decline in rent prices | X | | |
| Strength of main tenants | | | X |
| Competitive environment | X | | |
| Approvals from authorities | | | X |
| Environment and regulatory requirements | | X | |
| Changes in tax burden | | X | |
| Cyber risks | | X | |
| Specific Risks | | | |
| Fluctuations in the CPI | | X | |
| Foreign currency risks | | | X |
| Dependency on financing sources | | X | |
| Debt raising costs | | X | |
| Senior housing-specific risks | | | X |

Danna Azrieli,

Chairman of the Board

Eyal Henkin,

CEO

Report Date: March 19, 2019

# Board Report

# Part B

# DEAR SHAREHOLDERS,

2018 was an excellent year for the Azrieli Group, a year of continued development and growth in all of our core business segments.

This year, we experienced significant growth of the office segment, with considerable and vigorous demand by a large number of tenants. The world's largest companies, global leaders in their fields such as Amazon and Facebook, joined the remarkable selection of companies coming from the finance, high-tech and other industries, who lease from us tens of thousands of square meters at high rental prices. The lease-ups of the Azrieli Sarona Tower, Azrieli Rishonim project and the Azrieli Holon Center are particularly outstanding in this context. In December 2018 we were very proud to unveil the Group's next flagship project – the Spiral Tower. The Spiral Tower was designed in cooperation with international firm KPF Architects, and is expected to be Israel's tallest building. In line with the world's leading skyscrapers, the tower will include mixed uses. The project's plan reflects our superior and uncompromising building standard and I believe that upon its completion, the Spiral Tower will stand out as a unique, prominent and innovative project in Tel Aviv's skyline, offering a unique experience to its users and visitors.

In the malls segment we continue to lead thanks to our experience and professionalism, as well as the services and innovation we offer, and the prime locations of our malls nationwide. Our malls continue to demonstrate strength and stability and we are keeping up the highest shopper traffic level, for the benefit of our tenants, while continually maintaining a right mix of tenants, with considerable emphasis on leisure and entertainment. The Azrieli Group timely recognized the importance of integration between the physical and digital worlds, and entered the e-commerce business through our Azrieli.com website, which provides our tenants with an additional platform for these two worlds to interface. Furthermore, our App and Gift Card are proving themselves as tools that continue to grow and integrate into the dynamic world of e-commerce and provide users with innovative consumer solutions.

In the senior housing sector, the launch of our new, ravishing "Palace" project in Modi'in yet again demonstrates our prominent entrepreneurial advantage. Alongside the continued growth and successful operation of the two senior homes we acquired in previous years, in 2018 we launched the senior home "Palace Modi'in" which is the first senior housing project we developed and built from the ground up – from land acquisition to resident move-ins. Within less than six months from the opening of the project, the marketing and sales figures have far exceeded our forecasts. We have three additional projects under development in the senior housing segment, which continues to be one of our substantial growth engines.

Alongside our diverse business in Israel, the Azrieli Group continues to expand its income-producing property business with offices in the U.S., in locations where the Group has already established a solid presence, such as Houston, as well as in new, dynamic and promising business markets, such as Austin, Texas, where we have recently acquired another office building.

The Group's entrepreneurial DNA enables us to start 2019 with an outstanding pipeline of projects in various development stages, totaling hundreds of thousands of square meters, which will significantly contribute to the Group's growth in the coming years. In this context, the financial resilience of the Azrieli Group, as expressed in the past year in our low-interest rate, long-duration bond financings, is expected to be an anchor for our continued solid growth.

At the threshold of 2019, I am very optimistic; I have full faith in our meeting the goals which we had set for ourselves and am confident that we will continue to lead the market as the strongest income-producing property company in Israel.

Yours,

Danna Azrieli,
Chairman of the Board

Azrieli Group

# BUSINESS CARD

Azrieli Group focuses on income-producing real estate and is Israel's largest real estate company.

In the shopping malls sector, the Group holds several leading malls, including Azrieli Jerusalem mall, Azrieli Ayalon mall and Azrieli Tel Aviv mall. The Company also holds and manages office properties, including some of the most prominent in Israel, such as the Azrieli Tel Aviv Center and the recently completed Azrieli Sarona tower. The Company also operates in the senior housing sector and manages three active senior homes. In the United States, the Company holds several office buildings, mainly in Houston and Austin, Texas.

Azrieli Group has an extraordinary pipeline of hundreds of thousands of square meters of office, retail and senior housing space in projects under development or under construction, which will contribute significantly to the Group's future growth. In addition, we constantly invest in the preservation of the quality and value of our current property portfolio.

In addition to its real estate business, the Group has other holdings and activities: The Azrieli.com e-commerce platform; alternative energy marketing company Supergas; and water, wastewater treatment and chemicals company GES (through the wholly-owned subsidiary Granite Hacarmel). The Company also has financial holdings in Bank Leumi (3.05% equity interest) and had financial holdings in Leumi Card (20% equity interest), which were sold in February 2019, as stated in Section 1.2.3.6 below.

Azrieli Group's financial strength puts it in a class of its own among real estate companies. The Company has a low leverage rate, with a net debt to assets ratio of approx. 28% only. We target the best locations for our properties, to provide good transportation access over time and form a significant part of their urban environment. The location and quality of the properties are planned to serve as the best platform for our malls' tenants and visitors. As Israel's leading and strongest real estate group, Azrieli Group intends to continue its real estate work, and lead the development and management of high-quality, modern and innovative income-producing properties in Israel and overseas.

We will act together in continuing to focus on the Group's core business, while investing in new growth engines and application of advanced technologies.

Established in 1983

NIS 3.3 billion dividend
since the IPO

Over 1.2 million sqm of leasable area
and close to 0.7 million sqm more under development

The biggest real estate company in Israel
NIS 31.9 billion total assets

99% occupancy rate*
on average in Israel

*Net of properties under lease-up

## 17 MALLS

335 thousand sqm | 98% Occupancy

## 14 OFFICE BUILDINGS

548 thousand sqm | 99% Occupancy*

## 3 SENIOR HOMES

76 thousand sqm | 794 residential units
100% Occupancy*

## 8 OFFICE BUILDINGS OVERSEAS

246 thousand sqm | 84% Occupancy

## DEVELOPMENT PIPELINE

10 properties | 680 thousand sqm

# PERFORMANCE SUMMARY AND FINANCIAL HIGHTLIGHTS FOR 2018

NOI **~10% up** (~NIS 1,523 million), compared to the same period last year (~NIS 1,385 million)

FFO attributed to the income-producing real estate business, excluding senior housing **~11% up** and FFO for the entire income-producing real estate business **~23% up**

Net profit from operations **~10% up** *
(~NIS 962 million in 2018, compared to ~NIS 878 million in the same period last year)

* Net profit excluding the effect of real estate revaluations net of tax, the effect of the change in the tax rate and dividends and profits from the holdings in Bank Leumi and Leumi Card.

Total assets **~6% up** (~NIS 31.9 billion in 2018, compared to ~NIS 30.1 billion in 2017)

**Decrease** of average interest rate and **extension** of average debt duration over the years

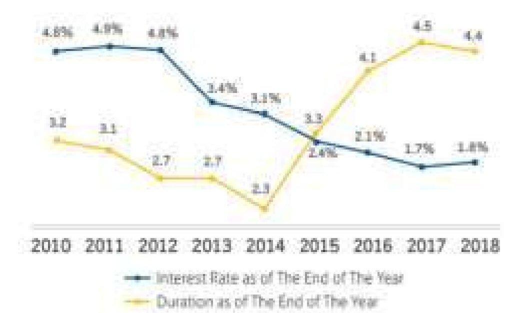
Dividend for distribution **~8% up** (NIS 560 million in 2018 compared to NIS 520 million in 2017)

NOI


FFO from Real Estate


Total Assets


Average Interest
Vs. Average Duration of Debt



# 1 | THE BOARD OF DIRECTORS' EXPLANATIONS ON THE STATE OF THE CORPORATION'S BUSINESS

## 1.1. General

The board of directors of Azrieli Group Ltd. (the "Company"; the Company jointly with all corporations directly and/or indirectly held thereby shall hereinafter be referred to as the "Group" or the "Azrieli Group") is proud to present this board of directors' report for the year ended December 31, 2018 and for the three-month period ended December 31, 2018 (the "Report Period"), in accordance with the Securities Regulations (Periodic and Immediate Reports), 5730-1970 (the "Regulations").

The information in the board of directors' report is based on the consolidated financial statements as of December 31, 2018[1]. The Company's financials and results of operations are affected by the financials and results of operations of the companies held thereby. In some cases, we present details of events that occurred subsequently to the date of the financial statements and shortly before the date of release of the report (the "Report Release Date"), while indicating the same, or additional figures and details that are strictly at Company-level. The materiality of the information included in this report has been examined from the Company's perspective. In some cases, an additional and detailed description is provided in order to provide a comprehensive picture of the described issue, which the Company believes to be material for the purposes of this report.

## 1.2. Key Figures from the Description of the Corporation's Business

### 1.2.1. Summary of Operating Segments for 2018

In 2018, the Azrieli Group continued to focus its business operations on various real estate sectors, primarily on the retail centers and malls in Israel segment and the leasable office (and other) space in Israel segment, as well as on the income-producing property overseas segment (mostly in the U.S.). The Company has also been active in the senior housing segment, the Granite segment (which mainly consists of the marketing of alternative energy sources and the treatment of water, wastewater, air, waste and chemicals for industry), as well as e-commerce. In addition, the Company holds minority interests in financial corporations. The Group's primary growth engine is the development of income-producing real estate projects: malls, offices and senior housing. As of the date of the Report, the Company has ten projects under various development stages in Israel, the planned area of which is approx. 680 thousand sqm, as well as land for development. A brief description of the Group's five reported operating segments, as well as its additional activities ("Others") follows:

1. Retail centers and malls in Israel – The Group has 17 malls and retail centers in Israel;
2. Leasable office and other space in Israel – The Group has 14 income-producing office properties in Israel;
3. Income-producing properties in the U.S. – The Group has 8 office properties overseas, mainly in the U.S.;
4. Senior housing – The Group has 3 active senior homes in Israel;
5. Granite – The Group holds a business for alternative energy sources marketing and a business of water, wastewater and chemicals treatment[2].

[1] The attached financial statements are prepared according to the International Financial Reporting Standards ("IFRS"). For further details, see Note 2A to the financial statements.

[2] The Group, through Granite Hacarmel Investments Ltd. ("Granite" or "Granite Hacarmel"), holds 100% of the rights in Supergas Israeli Gas Distribution Company Ltd. ("Supergas"), which markets alternative energy sources; and 100% of G.E.S. Global Environmental Solutions Ltd. ("GES"), the business of which is water, wastewater, air, waste and chemicals for industry treatment.

Additional activities – The Group holds an e-commerce business through the Azrieli.com website, as well as interests in financial corporations: approx. 3.05% of the shares of Bank Leumi LeIsrael Ltd. ("Bank Leumi") as of the Report Release Date and by February 25, 2019, held 20% of the shares of Leumi Card Ltd. ("Leumi Card")[3].

## 1.2.2. Breakdown of Asset Value by Operating Segment

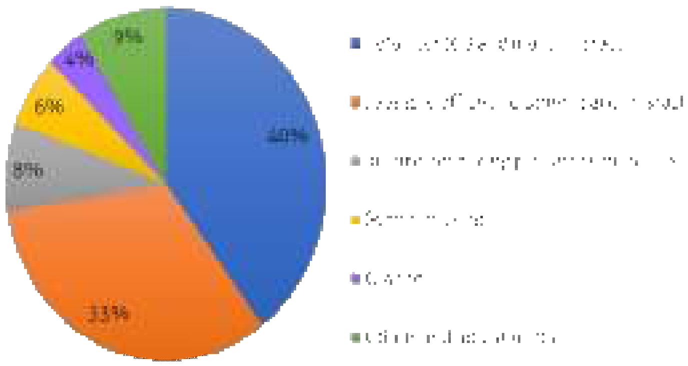
The following chart presents a breakdown of the total balance sheet assets by operating segment[4]:

**Breakdown of Total Balance Sheet Assets by Operating Segment**

| Comparison of Segment Assets to Prior Year | | |
|---|---|---|
| As of | 31.12.2018 | 31.12.2017 |
| Retail centers and malls in Israel | 12,682 | 12,368 |
| Leasable office and other space in Israel | 10,443 | 9,462 |
| Income-producing properties in the U.S. | 2,593 | 1,983 |
| Senior housing | 2,081 | 1,725 |
| Granite | 1,225 | 1,265 |
| Others and adjustments | 2,871 | 3,340 |
| Total | 31,895 | 30,143 |

Percentage of Segment Assets out of Total Assets

31.12.2018




Figures are presented in millions of NIS.

The retail centers and malls segment constitute approx. 40% of the total balance sheet assets. The other income-producing real estate segments constitute, in the aggregate, approx. 47% of the total balance sheet assets. In the Company's estimation, the relative share of retail centers and malls is expected to decrease over time, in view of the Group predominantly focusing its development efforts in the coming years on the office and senior housing segments.

## 1.2.3. Summary of the Main Developments during and after the Report Period

### 1.2.3.1. Closing the Acquisition of an Office Building in Austin, Texas, U.S.A.

In July 2018, the Company closed the acquisition of an office building in Austin, Texas, U.S.A., in consideration for approx. U.S. $100.4 million. The purchased property is a 5-floor office building with a total area of approx. 23,214 sqm (approx. 249,870 sq ft) and an occupancy rate of approx. 100%. The property also includes approx. 970 parking spaces, most of which are situated in a nearby 7-floor car park.

[3] For details on the sale of the Group's full holdings in Leumi Card, see Section 1.2.3.6 herein.

[4] The Company applied IFRS 8 – Operating Segments in its financial statements.

### 1.2.3.2. Engagement in an Agreement for the Purchase of Rights to Land on Menachem Begin Road, Tel Aviv

In May 2018, the Company closed the purchase of rights to land located on Menachem Begin Road, Tel Aviv, holding a 4-floor building over a commercial ground floor, in the total area of approx. 5,500 sqm and underground floors mostly leased for office purposes. The property includes unutilized building rights according to the zoning plan that applies to the land at a total scope of approx. 21,000 sqm, above-ground, and additional rights. In consideration for the purchase of rights to the land, the Company paid the sum of NIS 260 million.

### 1.2.3.3. Winning of a Tender for the Construction of a Facility for Waste Storing and Recycling and Energy Production in the Rishon LeZion Area

On April 10, 2018, notice was received by Zero Waste Ltd. (“Zero Waste”), a corporation held by GES in equal shares with Shikun & Binui (“Shikun & Binui”), whereby Zero Waste was the chosen winner of a BOT tender for the planning, funding, construction and operation of a facility for the sorting and recycling of municipal waste and energy production (the “Project”), which was issued by the Ministry of Finance (the Accountant General) and the Ministry of Environmental Protection. The Project will be built in the area of the Dan Region Wastewater Treatment Plant (the Shafdan) in Rishon LeZion and its cost during the construction period is estimated at approx. NIS 750 million. The execution of the Project is subject to the completion of a financial closing of the Project. On July 2, 2018, the Company updated that Zero Waste received a petition of another group that contended in the same tender, in which the Jerusalem District Court is moved, *inter alia*, to reverse the Tender Committee’s decision to choose Zero Waste as the winner of the tender, and determine that the other group is the winner of the tender, or alternatively remand the case to the Tender Committee to review Zero Waste’s compliance with the tender’s requirements. On February 14, 2019, the Court's decision was given, denying the petition with no award of costs.

### 1.2.3.4. Winning of a Tender for the Purchase of Land in Modi’in (Lot 21)

On January 11, 2018, the Group won a tender held by the Israel Land Authority for the purchase of long-term lease rights in a lot located in the CBD of Modi'in-Maccabim-Re’ut, on an area of approx. 5,300 sqm, designated for the construction of 80 residential units, 50 hotel rooms, offices and retail space, in consideration for approx. NIS 101.5 million.

### 1.2.3.5. Sale of Pi Glilot Land

On May 10, 2016, the Company and Granite, including through Sonol, sold all of their holdings in Pi Glilot land and in the shares of Pi Glilot (which holds a leasehold with respect to land in the Pi Glilot site) to third parties for total consideration of approx. NIS 130 million. In the Report Period, the transactions were closed and the consideration in respect thereof was paid in accordance with the provisions of the sale agreements.

### 1.2.3.6. Sale of the Company’s Holdings in Leumi Card

The Company and Bank Leumi entered into an agreement for the sale of all of their holdings in Leumi Card to a corporation controlled by the investment fund Warburg Pincus, for the consideration of NIS 2,500 million (in this section: the “Agreement”). The Company’s share in the proceeds is NIS 500 million (subject to adjustments). On February 25, 2019, the transaction was closed and the consideration for that phase was received in accordance with the provisions of the Agreement.

### 1.2.3.7. Changes in Officer Positions in the Company

Mr. Eyal Henkin was appointed as the Company's CEO and his office commenced on January 1, 2018. Prior to his appointment to this office, he had served as the CEO of Supergas for some eight years.

In August 2018, Ms. Rachel Mittelman was appointed as the Group's Chief Information Officer, beginning September 2018.

In February 2019, Mr. Assaf Aviv was appointed as the Group's VP Innovation and Business Development, beginning March 2019.

### 1.2.3.8. Extension of the Term of the Shelf Prospectus

On March 21, 2018, the Israel Securities Authority (ISA) extended the term of the Shelf Prospectus by 12 additional months, i.e., until May 11, 2019.

Concurrently with the submission of this Report, the Company shall submit a first draft of a new shelf prospectus to the ISA.

### 1.2.3.9. Engagement of Supergas Natural in an Agreement with a Third Party for the Purchase of Natural Gas

For details regarding the engagement of Supergas Natural in an agreement with a third party for the purchase of natural gas, see Note 29B(4) to the financial statements.

### 1.2.3.10. Financing Transactions

During Q1/2018, the Company expanded the D Bond Series.

After the Report Period, in January 2019, the Company issued two new bond series of the Company (Bond Series E and F), such that Series E Bonds of approx. NIS 1,216 million par value were allotted in consideration for approx. NIS 1,216 million (approx. NIS 1,207 million net of the issue expenses), and Bonds Series F of approx. NIS 263 million par value were allotted in consideration for the amount of approx. NIS 263 million (approx. NIS 260 million, net of the issue expenses).

For details on the bond series expansion and issuance of new bonds, see Section 19.5 of Chapter A herein.

### 1.2.3.11. Litigation

For an update with respect to the main legal proceedings to which any of the Group's companies is a party, see Note 31 to the financial statements, Part C herein.

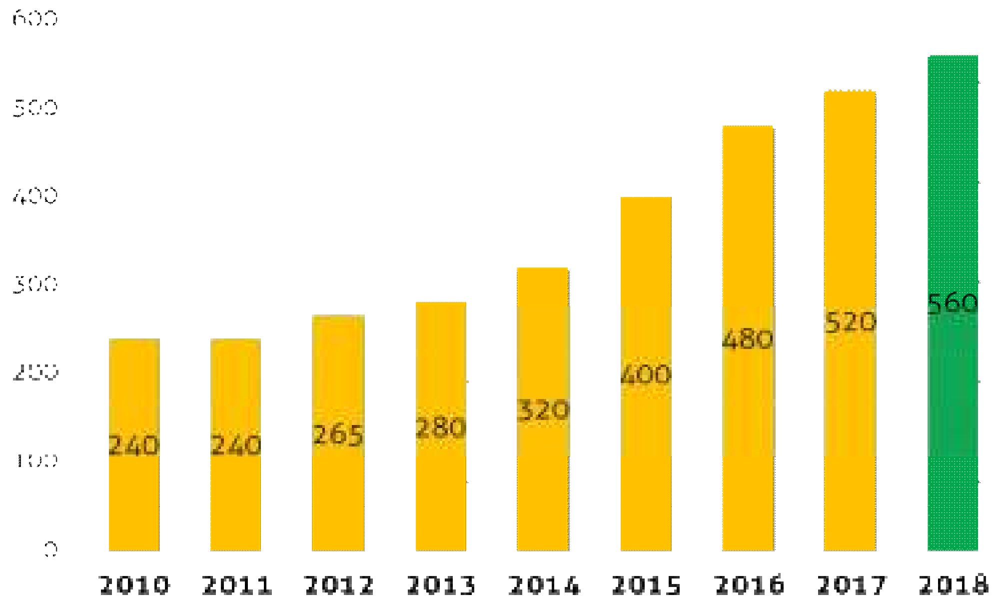
### 1.2.3.12. Income Tax assessments

In the Report Period, a settlement agreement was signed between the Company and Canit Hashalom Investments Ltd., with the Israel Tax Authority in respect of tax assessments. According to the settlement agreement, the Company shall pay amounts, most of which will be returned to the Company in the coming years as a deduction from future tax liability (timing differences). The Settlement Agreement had no material effect on the Company's financial results. For further details, see Section 1.3.11 of Chapter A herein and Note 28F to the Financial Statements.

### 1.2.4. Dividends

Since its public offering, the Company has distributed annual dividends in increasing amounts. The amount of the annual dividend has increased by approx. 133% in the past eight years. The total aggregate amount distributed by the Company since the listing of its shares in 2010 is approx. NIS 3.3 billion, including a dividend for 2018, which has been declared, but not yet paid. The following chart specifies the amounts of the dividends distributed in recent years:

**Dividends Distributed by the Company since Listing its Shares on TASE**




Figures are presented in millions of NIS.
The years noted represent the years for which dividends were distributed. Dividends were actually paid in March of the following year.
The dividend for 2018 has been declared but not yet paid.

# 2 | INCOME-PRODUCING REAL ESTATE

2 |

## 2.1. Business Environment

In the estimation of the Company's management, there has been no material change in the business environment in which it operates, as described in last year's board of directors' report (as of December 31, 2017). Following are macroeconomic indicators that are relevant to all of the operations in Israel, based on the publications of the Central Bureau of Statistics[5]:

- According to the macro-economic forecast of the research division of the Bank of Israel of January 2019, the indicators of the market's activity show that the Israeli market is continuing to grow. In 2018 the growth rate is expected to reach approx. 3.4% and growth at the same rate is expected in 2019.
- As of the beginning of 2019, Israel's population is approx. 9 million. The population growth rate is among the highest in OECD countries at approx. 1.9% per year (thanks to the high birth rate and an increase in life expectancy). According to population growth forecasts, in the middle of the next decade Israel's population will total approx. 10 million, and in 2035 Israel will have more than 12 million residents.
- The workforce unemployment rate is low at approx. 4.3%, as of January 2019.
- The (known) Consumer Price Index (CPI) increased by approx. 1.2% in 2018. The Bank of Israel interest rate is up this year and as of the Report Release Date, is 0.25%.
- The Prime interest rate is up 0.15% to a rate of 1.75%.
- As set forth in detail below, the income-producing real estate sector in Israel maintained stability in 2018 both in terms of demand and in terms of rent levels and occupancy rates, continuing the trend that characterized 2017.

The Company's management estimates that various factors in the Group's strategy contribute to a reduction of the exposure of the Group's business to a significant crisis or to instability resulting from the materialization of any of the Company's risk factors:

- The broad dispersion of the Group's real estate portfolio, both geographically and among its various operating segments.
- The portfolio features numerous properties located in areas of demand, which are built and maintained to very high standards.
- The high business positioning of the properties and the Company's investments in the betterment of its properties to maintain this advantage.
- The high occupancy rates, which result from the aforementioned factors.
- The diversity of businesses in the Group's malls and retail centers, which reduce the Group's exposure to such or other sector.
- The right mix of businesses, which characterizes the tenants at the retail centers and in the offices.
- Finally, the Company's stable capital structure and its financial conservativeness allow it to more easily weather fluctuations in business turnovers and profitability.

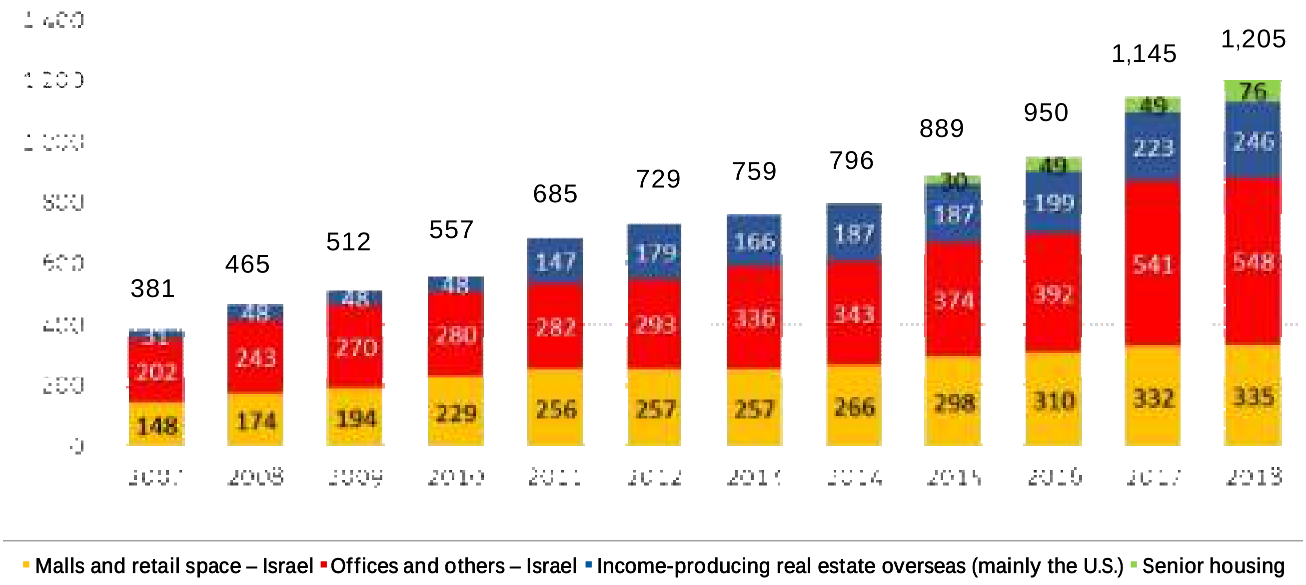
*The Group's aforesaid estimations with regards to the changes in the income-producing real estate sector in Israel and their effect on the Group's results are merely subjective estimations and constitute forward-looking information, within the definition of this term in the Securities Law, 5728-1968 (the "Securities Law"). Actual*

[5] Central Bureau of Statistics www.cbs.gov.il

*results and effects may materially differ from the aforesaid estimations and what they imply, for various reasons, including the further intensification of competition, a decline in demand and a deterioration of the Israeli economy.*

## 2.2. Consolidated GLA Data

GLA Breakdown as of the End of 2018




Figures present thousands of sqm.

## 2.3. Average Occupancy Rates in the Income-Producing Properties

As of the Report Date, following are the average occupancy rates in the Group's income-producing properties by operating segment:

- Retail centers and malls in Israel – approx. 98%;
- Leasable office and other space in Israel – approx. 99%;[6]
- Income-producing properties in the U.S. – approx. 84%;
- Senior housing in Israel – 100%[6].

## 2.4. NOI of the Properties

Net Operating Income (NOI) is a measure that presents the net operating income of the properties: income after the deduction of the property's operating expenses and prior to the deduction of taxes and interest. It serves as one of the important parameters in the valuation of income-producing real estate companies, as its division by the appropriate cap rate for the properties provides an indication for the determination of the value of the income-producing properties.[7] In addition, after deduction of the current maintenance expenses incurred to preserve the property's condition, NOI is used to measure the free and available cash flow for the service of financial debt undertaken for the purpose of funding the purchase of the property.

We wish to emphasize that these parameters do not present cash flows from current operations according to generally accepted accounting principles, nor do they reflect cash available for the funding of all of the Group's cash flows (including its ability to make distributions), and they are not meant to be deemed as a substitute for net profit in the evaluation of the results of the Group's operations.

[6] Excluding areas in properties whose construction has been completed and are being leased-up for the first time.

[7] Additional indications are, for example: The market value of similar properties in the same area and the sale prices of similar properties in recent transactions.

### 2.4.1. NOI Data

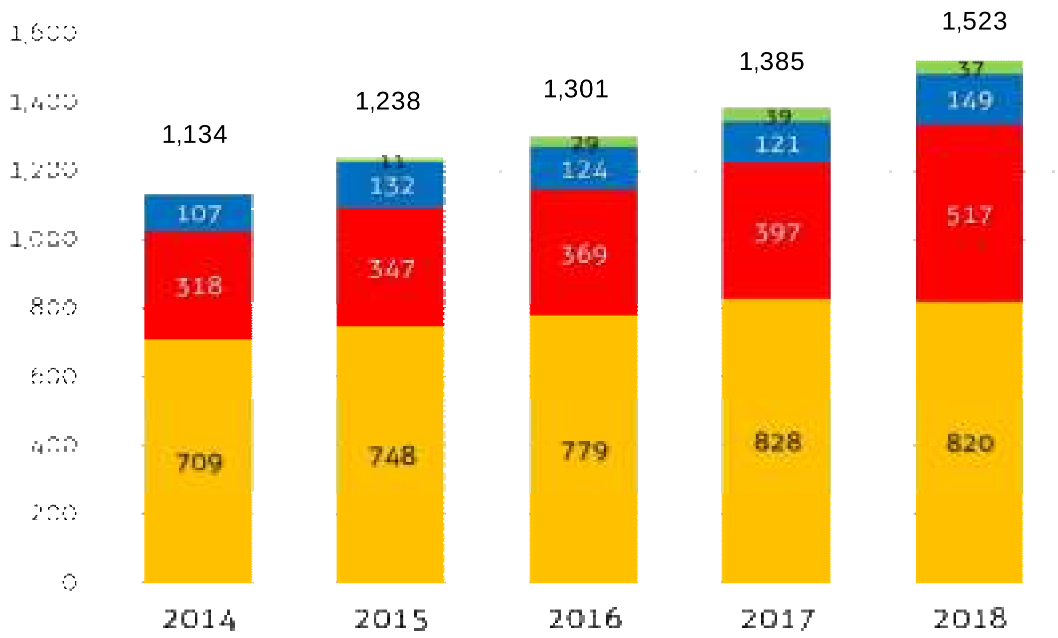
For the purpose of calculating the NOI, on the revenues side – all proceeds from tenants are taken into account (including rent, management fees and other payments), and for the purpose of calculating the costs – all operating expenses in respect of the properties are taken into account (including management, maintenance and other costs).[8]

During the last decade, the Group recorded constant growth at an average annual rate of 9.14%, and an overall increase in the years 2008-2018 of approx. 140% in actual NOI figures in all of its income-producing real estate segments, in both Israel and abroad.

The NOI figures for the income-producing real estate portfolio are as follows:

NOI

Annual Data




▪ Retail centers and malls in Israel ▪ Leasable office and other space in Israel ▪ Income-producing properties in the U.S. ▪ Senior housing

Figures are presented in millions of NIS.

For explanations with respect to the change in NOI, see Sections 2.10.2, 2.11.2, 2.12.2 and 2.13.2 herein.

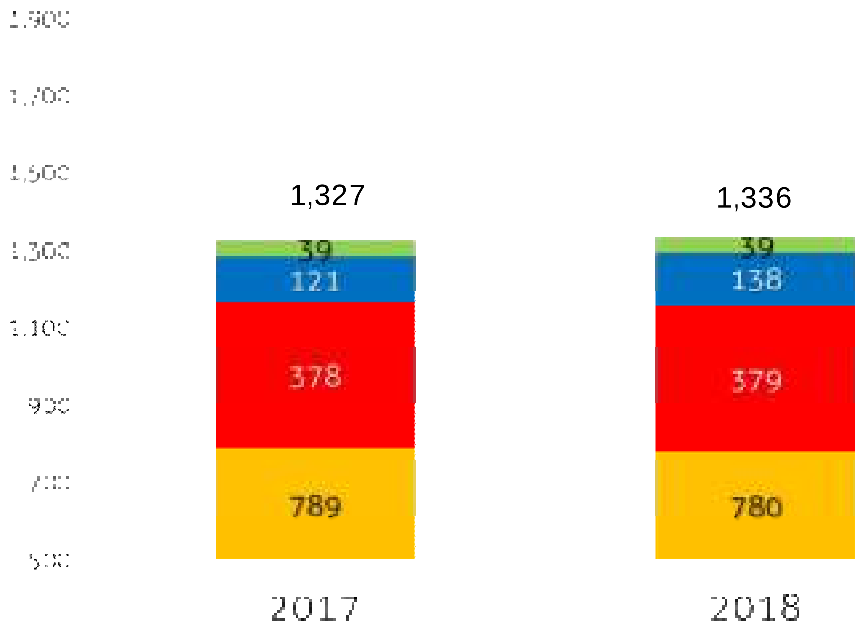
### 2.4.2. Same-Property NOI Data

The NOI indicator is affected by changes in the portfolio. That is to say, the sale of a property or the addition of a new property to the Company's portfolio is reflected in a change in the NOI. Contrarily, the Same-Property NOI indicator discounts such changes and allows for an examination of changes in the profitability of the same portfolio of the Group over time. For the purpose of calculation thereof, only properties that were part of the Group's portfolio throughout the analysis period are taken into account. In the years 2017-2018, this measure was as follows:

[8] The Group prepares its financial statements based on international standardization, and consequently, in the calculation of the cost of leasing and operating the properties classified as investment properties, depreciation was not taken into account. Furthermore, for the purpose of calculating the aforesaid parameters, profit from the revaluation of properties was not taken into account.

## Same-Property NOI

Annual Data




▪ Retail centers and malls in Israel ▪ Leasable office and other space in Israel ▪ Income-producing properties in the U.S. ▪ Senior housing

Figures are presented in millions of NIS.
Same-property NOI includes the office buildings in Houston, Texas U.S.A., in which the Company's holding rate has increased (see Section 2.13.2 herein)

Same-Property NOI rose by approx. 1% between the years 2017 and 2018. Such rise derived from an increase of approx. 14% in the income-producing properties in the U.S. segment (see Section 2.13 below) offset by a decrease in the retail centers and malls segment, and with stability in the leasable office and other space segment and the senior housing segment. The difference between the NOI and Same-Property NOI mainly derives from the opening of the Rishonim project in March 2017, the opening of the offices in Sarona in July 2017, the impact of the vacation of an income-producing property as part of the preparation for the excavation work in the Lodzia site, the purchase of the property at Menahem Begin Road in Tel Aviv, in May 2018 and the purchase of the office building in Austin, Texas, U.S.A. in July 2018.

## 2.5. Extended Standalone Statement – the Income-Producing Properties Business

The Company's management acknowledges the importance of transparency to investors, shareholders, bondholders and analysts, and views all of them as its partners. The Company has thus decided to adopt a policy, whereby the board of directors' report will include disclosure of a summary of the Company's extended standalone financial statements, i.e., a summary of the Company's consolidated balance sheets and income statements presented according to the IFRS rules, excluding the Company's investments in Granite Hacarmel and Azrieli E-Commerce Ltd. ("Azrieli E-Commerce")[9], which are presented based on the equity method *in lieu* of consolidation of their statements with the Company's statements (the other investments are presented with no change to the statement presented according to the IFRS rules). The Company's management believes that this statement adds extensive information, which assists in the understanding of the real estate business's vast contribution to the Company's total profit, while discounting material items in the consolidated financial statements that stem from the consolidation of Granite Hacarmel and Azrieli E-Commerce, such as trade receivables, inventory, sales and more.

[9] The company formerly known as Netex New Media Ltd., which was acquired by the Company in a transaction for the acquisition of an e-commerce business. For details see Section 14.1 of Chapter A herein.

The extended standalone statement is attached hereto as Annex B. Such statement is neither audited nor reviewed by the Company's accountants.

## 2.6. Weighted Cap Rate

The following table shows the calculation of the weighted cap rate derived from all of the Group's income-producing real estate, excluding senior housing[10], for 2018:

| Calculation of the Weighted Cap Rate for 2018 | |
|---|---|
| Total investment properties in the "Extended Standalone" statement (1) | 27,596 |
| Net of value attributed to investment properties under construction | (2,458) |
| Net of value attributed to land reserves | (497) |
| Net of value attributed to income-producing senior housing | (1,687) |
| Total value of income-producing investment properties (including the fair value of vacant space) | 22,954 |
| Actual NOI in the quarter ended December 31, 2018 (excluding senior housing) | 382 |
| Additional future quarterly NOI (2) | 37 |
| Total standardized NOI | 419 |
| Proforma annual NOI based on the standardized NOI (excluding senior housing) | 1,676 |
| Weighted cap rate derived from income-producing investment properties (including vacant space) (3) | 7.3% |

Financials are presented in millions of NIS.

(1) Extended Standalone Statement – See Annex B. According to valuations which were received for December 31, 2018. The figure includes receivables that appear under the balance sheet item "Loans and Receivables" for averaging attributed to real estate.

(2) The figure includes adjustment to NOI as included in the valuation as of December 31, 2018 and therefore includes, *inter alia*, additional NOI for vacant space which was not yet fully occupied and space occupied over the course of 2018 under a whole-year lease (the main amounts in this item are due to tenant move-ins at the offices in Azrieli Sarona Center in Tel Aviv, in Azrieli Holon center, tenant move-ins at Azrieli Rishonim and due to the Group's properties overseas).

(3) Standardized annual NOI rate out of total income-producing investment properties (including vacant space). For the test of sensitivity to changes in the cap rate interest of investment properties, see Annex A to this chapter.

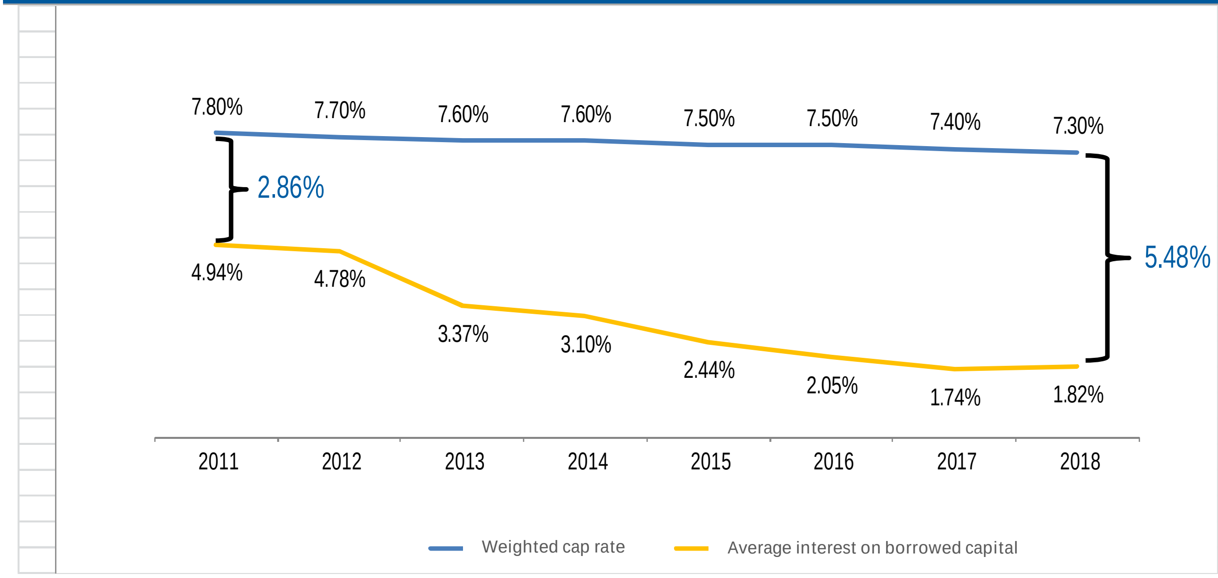
This figure does not constitute the Company's NOI forecast for 2019 and its entire purpose is to reflect the NOI assuming full occupancy for a whole year of all income-producing properties.

*The Company's estimations in this Section include forward-looking information, within the definition of this term in the Securities Law. This information is uncertain and it is based, inter alia, on information pertaining to contractual engagement with tenants as of the date of the Report, parameters in the calculation of fair value and the Company's estimations regarding space occupancy. Actual results may materially differ from the aforesaid estimations and what they imply, for various reasons, including immediate cancelation of lease agreements or a business crisis of any one of the tenants, or a change in the fair value parameters or failure to meet the development or occupancy goals.*

In recent years, the weighted cap rate of the Group's properties has only slightly decreased, despite the considerable decrease in the market interest rate in recent years. On the other hand, consistently with such decrease of the market interest rate, the Group's financing costs have significantly dropped in recent years. Therefore, recent years have seen major gaps between the weighted cap rate of the Group's properties and the financing costs, as depicted in the following chart:

[10] Since the value of senior housing properties is derived from the FFO indicator, rather than the NOI indicator, such properties were not included in this calculation. The weighted senior housing cap rate as of the date of the Report is 8.75%.

## Gap between the Weighted Cap Rate and the Average Interest Rate of the Debt




Figures are accurate as of the end of each year.

## 2.7. Real Estate Business FFO

Funds from Operations (FFO) is a measure that presents the cash flow from the real estate business. It is commonly used worldwide and provides a proper basis for the comparison of income-producing real estate companies. This indicator reflects income from net profit, discounting revenues and expenses of a capital nature and adding the Company's share in real estate depreciation and other amortizations.

This report presents the FFO indicator in respect of the Group's income-producing real estate business.

It should be stressed that the FFO indicator does not reflect cash flow from current operations according to generally accepted accounting principles, nor does it reflect cash held by the Company and its ability to distribute the same, and it is not a substitute for the reported net profit. It is further clarified that this indicator is not a figure audited by the Company's accountants.

| FFO from the Income-Producing Real Estate Business | | | |
|---|---|---|---|
| | 31.12.2018 | 31.12.2017 | 31.12.2016 |
| Net profit for the period attributable to shareholders | 1,218 | 1,456 | 1,810 |
| Net of the profit, net, from Granite Hacarmel and Azrieli E-Commerce attributable to the shareholders (including a deduction of excess cost) | (19) | (20) | (10) |
| Profit adjustments (1): | | | |
| Increase in the value of investment properties | (220) | (510) | (716) |
| Depreciation and amortizations | 9 | 7 | 9 |
| Net financing and other non-cash flow expenses (revenues) | 66 | (169) | (80) |
| Tax expenses (revenues) | 132(7) | 253 | (117) |
| Net of a dividend received from financial assets available for sale | (91) | (33) | (10) |
| Cash flow from the receipt of residents' deposits net of deposits returned to residents(2) | 171 | 47 | 59 |
| Net of revenues from the forfeiture of residents' deposits | (22) | (21) | (17) |
| Total profit adjustments | 45 | (426) | (872) |
| Plus interest paid for real investments(3) | 10 | 13 | 20 |
| Total FFO attributed to the income-producing real estate business(4)(5) | 1,254 | 1,023 | 948 |
| Total cash flow of financing of properties under development(6) | 44 | 38 | 56 |
| Total FFO attributed to the income-producing real estate business, excluding the cash flow of financing of properties under development | 1,298 | 1,061 | 1,004 |

Financials are presented in millions of NIS.

(1) The below profit adjustments do not include adjustments in respect of Granite Hacarmel and Azrieli E-Commerce, as their results have been fully discounted.

(2) Senior housing residents' deposits are deemed received or returned on the date on which the agreement is signed or terminated, as applicable.

(3) Calculated according to the Group's weighted interest for the real investments, which include: Granite Hacarmel, Azrieli E-Commerce, Bank Leumi and Leumi Card, for 65% of the cost of the investments.

(4) Attributable to shareholders only.

(5) Including FFO from the senior housing segment in the sum of approx. NIS 165 million in 2018, in the sum of approx. NIS 45 million in 2017 and in the sum of approx. NIS 54 million in 2016.

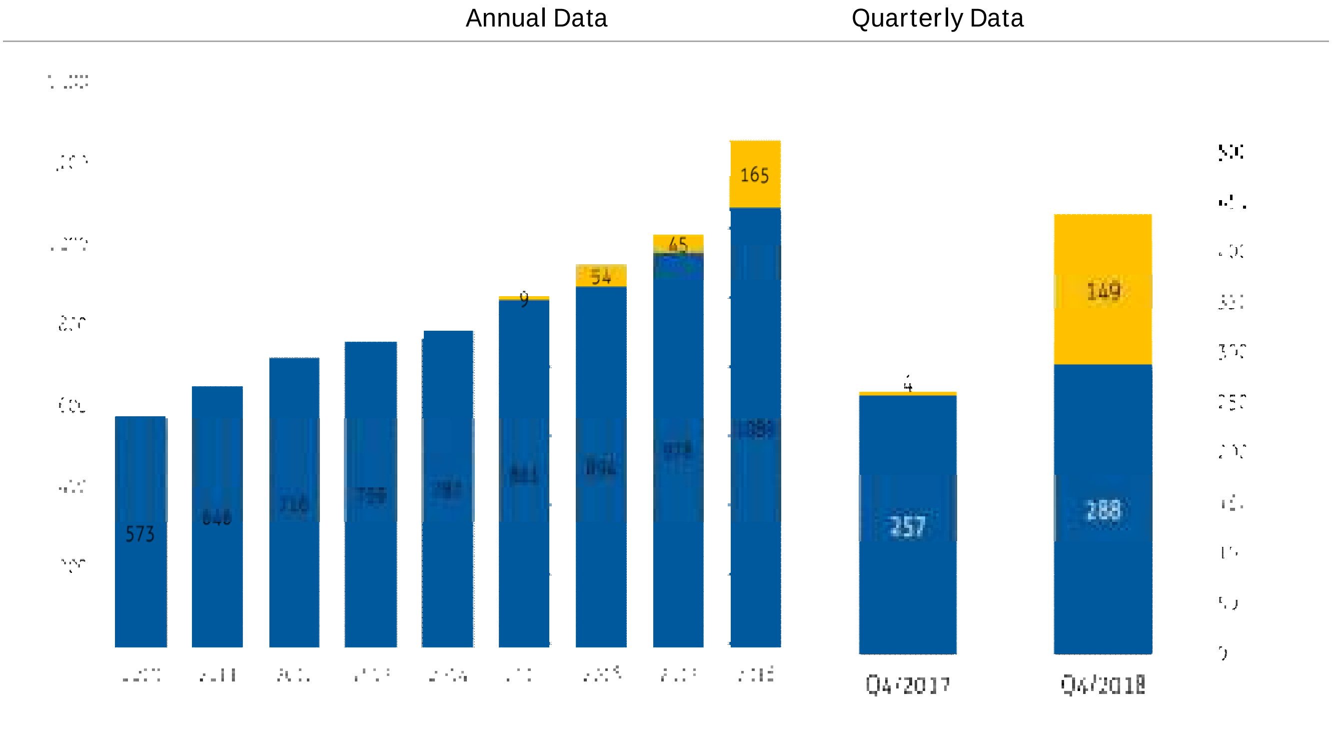
(6) Calculated on the basis of credit costs which were capitalized to qualified assets and investment property under construction in the financial statements.

(7) Including approx. NIS 109 million one-time tax expense in respect of an assessment agreement.

The FFO calculation also includes cash flow financing costs with respect to projects under construction.

In recent years, the Azrieli Group's FFO has been on a constant rise, growing from year to year. From the date of the Company's IPO (some eight years ago) the FFO of the income-producing real estate business rose by approx. 119%: From NIS 573 million in 2010 to NIS 1,254 million in 2018. The following chart depicts the development of the FFO of the Group's income-producing real estate business in recent years.

## FFO from the Income-Producing Real Estate Business in Recent Years




Figures are presented in millions of NIS
□ excluding the contribution of senior housing □ the contribution of senior housing

## 2.8. The EPRA (European Public Real Estate Association) Indices

The Azrieli Group is the only Israeli real estate company included in the EPRA indices. EPRA is an organization that brings together the public income-producing real estate companies in Europe. Being listed in the EPRA indices, provides the Azrieli Group greater exposure to international investors, according to its weight in the index.

In view thereof, the Group has decided to adopt the position paper published by EPRA with the purpose of improving the transparency, uniformity and comparability of financial information reported by real estate companies listed in the index. A report regarding two financial measures calculated according to such position paper follows.

It is emphasized that the following measures exclude the component of expected profit from projects under construction not yet recorded in the financial statements.

These figures do not constitute a valuation of the Group, are not audited by the Group's accountants and are not a substitute for the figures contained in the financial statements.

### 2.8.1. EPRA NAV

The EPRA NAV (Net Asset Value) is a measure that reflects the Group's net asset value on an ongoing, long-term basis, assuming no disposal of real estate, and thus requires certain adjustments, such as presentation according to the fair value of assets that are not so presented in the financial statements and the exclusion of deferred taxes resulting from the revaluation of investment properties.

It is noted that all development properties are included at their present value, i.e., based on the fair value of the land including investments in the properties, and no value is attributed to future revenues from such properties when occupied and producing income.

| EPRA NAV | | |
|---|---|---|
| | 31.12.2018 | 31.12.2017 |
| Equity attributable to the Company's shareholders in the financial statements | 17,077 | 16,281 |
| Plus a tax reserve in respect of the revaluation of investment properties to fair value (net of minority interests) | 3,241 | 3,044 |
| EPRA NAV | 20,318 | 19,325 |
| EPRA NAV per share (NIS) | 168 | 159 |

Figures are presented in millions of NIS, unless otherwise noted.

### 2.8.2. EPRA NNNAV

The EPRA NNNAV is a measure that reflects the Company's net asset value assuming the immediate disposal ("Spot") of the real estate business, and thus requires certain adjustments, such as presentation according to the fair value of assets and liabilities that are not so presented in the financial statements and adjustments to deferred taxes.

| EPRA NNNAV | | |
|---|---|---|
| | 31.12.2018 | 31.12.2017 |
| EPRA NAV | 20,318 | 19,325 |
| Adjustment of assets to fair value (excluding minority interests) | 15 | 19 |
| Adjustment of financial liabilities to fair value (excluding minority interests) | (103) | (324) |
| Net of a tax reserve in respect of the revaluation of investment properties to fair value (net of minority interests) | (3,241) | (3,044) |
| EPRA NNNAV | 16,989 | 15,976 |
| EPRA NNNAV per share (NIS) | 140 | 132 |

Figures are presented in millions of NIS, unless otherwise noted.

## 2.9. Existing properties portfolio

# AZRIELI GROUP'S INCOME PRODUCING REAL ESTATE*

## MALLS & SHOPPING CENTERS

Ayalon Mall
Hod Hasharon Mall
Herzliya Outlet
Givatayim Mall
Jerusalem Mall
Modi'in Mall
Azrieli Mall
Azrieli Holon Center
Holon Mall
Ramla Mall
Azrieli Ra'anana
Haifa Mall
Akko Mall
Kiryat Ata Mall
Or Yehuda Outlet
Hanegev Mall
Rishonim Mall

## OFFICES & OTHERS in Israel

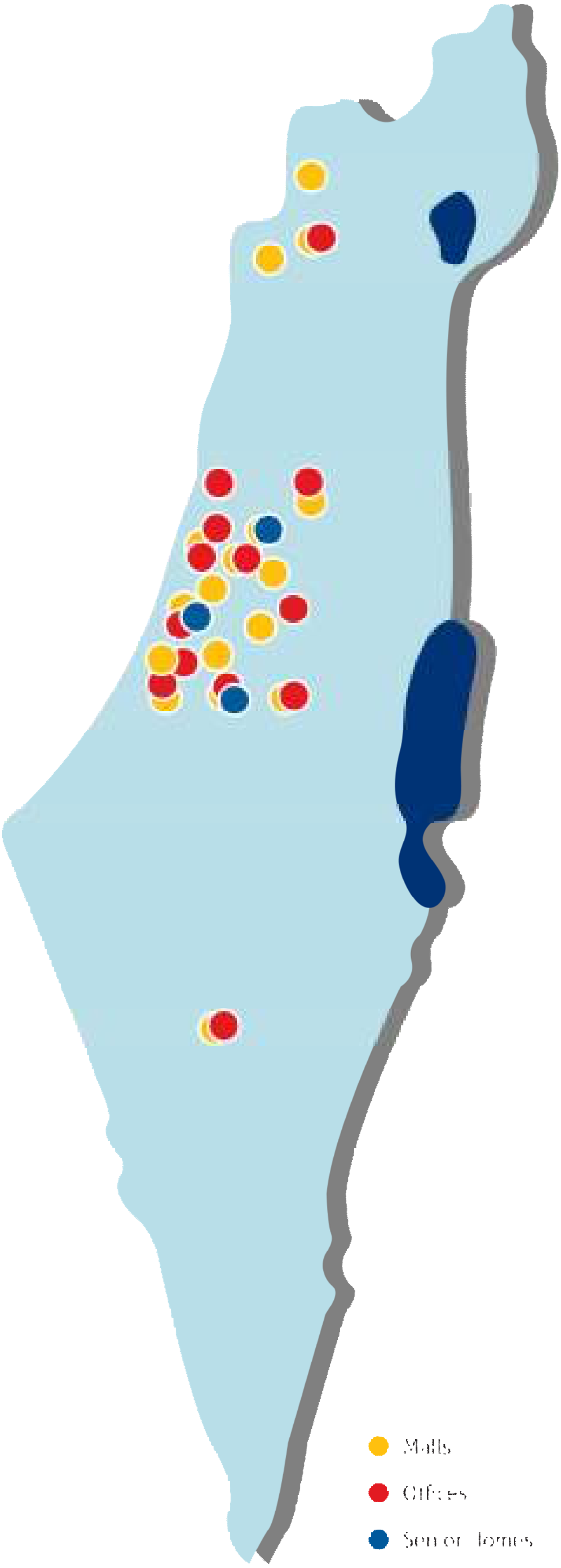
Azrieli Towers
Azrieli Sarona
Azrieli Holon Center
Caesarea
Herzliya
Modi'in
Modi'in Residences
Petach Tikva
Jerusalem
Givatayim
Kiryat Ata
Hanegev
Rishonim
Azrieli Town Building E

## OVERSEAS

GALLERIA
PLAZA
8 WEST
3 Riverway
1 Riverway
LEEDS
Aspen Lake II
San Clemente

## SENIOR HOMES

Palace Tel Aviv
Palace Ra'anana
Palace Modi'in




| | |
|---|---|
| 17 malls | 335,000 sqm |
| 14 office properties | 548,000 sqm |
| 3 senior homes | 76,000 sqm 794 residential units |
| 8 office properties overseas | 246,000 sqm |
| Total | 1,205,000 sqm |

*As of December 31, 2018

## 2.10. Retail Centers and Malls in Israel Segment

### 2.10.1.Description of the Retail Centers and Malls in Israel Segment

Retail centers are, and will continue to be, a significant part of the retail market in Israel. Malls and large retail centers in Israel provide customers with a more diverse shopping experience and a vast mix, including, *inter alia*, fashion chains and various attractions for the whole family, restaurants and cafés – all gathered under one roof, in accessible locations close to public transportation and with convenient car parking, unlike other types of retail areas, which lack some of the aforesaid features.

Private consumption in Israel, as well as the business activity in malls, is expected to continue growing, on the background of fast growth of the population and the household expenditure and despite the increase in online shopping and the "open skies" policy which reduced the prices of international flights.[11]

According to data from the Central Bureau of Statistics (CBS), Israel's populations is quickly growing at an annual average rate of approx. 1.9% per year (approx. 50 thousand new households in Israel each year),[12] a rate which far exceeds the population growth rate in developed countries. In addition, private consumption in Israel has demonstrated a fast growth rate in recent years of approx. 3.9% in 2018 and approx. 3.4% in 2017, in fixed prices.[13] As part of the growth in private consumption the household annual expense for consumption also grew, including the expense on clothing and footwear, and on entertainment.[14] It is emphasized that the ratio of retail space per capita in Israel is approx. 1.1 sqm per capita, smaller than the same ratio in many developed countries (such as the U.S., wherein the ratio is approx. 5 sqm per capita).[15]

The Azrieli Group owns and manages a portfolio of high-quality malls and retail centers throughout the country, which are located in city centers, with convenient access to transportation and often in proximity to train stations. The Company takes a long-term view with respect to its properties, from the stage of locating the land, through the stage of development and construction of properties, to the holding, management and betterment of the properties over years.

The Group's malls are mostly characterized by the following:

- Diverse and changing mix – the malls segment has a dynamic retail mix that is renewed according to the market needs and public preferences. For example, malls were once characterized by significant presence of supermarkets or electronics stores, whereas today the tenant mix in malls has changed. In fashion it is evident that new brands periodically take the place of those which have become less relevant, with international fashion chains becoming more dominant in the market than local brands. The high-quality property portfolio, and the management thereof, grant the Company an advantage which enables it to get leading international fashion brands to open their flag stores in the Group's malls.
- A trend of increased store space – increased retail space is recently demanded by international brands, followed by domestic ones, which seek to combine complementing brands in one store in order to expand the product mix and create an improved customer experience, while increasing the sales.
- Malls as entertainment venues – the Company acts to improve the entertainment and dining experience in the mall, through a selection of restaurants and cafés in the malls and renovation of the fast food courts, modern design and added crowd-attracting entertainment options such as the "Zappa" club. The Group further acts to create family entertainment spaces in its malls, including play areas, diaper changing and nursing rooms.

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[11] Geocartography, figures from a comprehensive research for the Azrieli Group on the retail sector in Israel, March 2018

[12] CBS – population data http://cbs.gov.il/publications18/yarhon0218/pdf/b1.pdf

[13] Israel's national accounts for 2018, CBS, published on March 10, 2019: http://cbs.gov.il/reader/newhodaot/hodaa_template.html?hodaa=201808069

[14] Geocartography analyses of the surveys on household expenditures in israel http://cbs.gov.il/webpub/pub/text_page.html?publ=25&CYear=2015&CMonth=1

[15] Geocartography, figures from a comprehensive research for the Azrieli Group on the retail sector in Israel, March 2018

- Innovation – in recent years the Company has been implementing technological improvements into the shopping experience and striving for leadership and innovation in the mall segment, including by way of creating a unique application which grant exclusive discounts to mall attendants and enables direct marketing based on customer preferences. The goal of technological innovation is to enhance customer experience in the mall while combining both digital and physical worlds.

The retail space in the malls and retail centers of Azrieli Group are leased to some 1,900 different tenants.

E-commerce operations – another element of the Group's Digital operations is the Azrieli.com website, which provides a platform for e-commerce that integrates into and enhances the operations of malls and retail centers through online operations, by way of combined sales.

## 2.10.2.Performance of the Retail Centers and Malls in Israel Segment and changes in Value

The Azrieli Group owns 17 malls and retail centers in Israel, in a total GLA of approx. 335 thousand sqm.

Balance of the properties of the retail centers and malls in Israel segment – in 2018, the balance of investment property in this segment increased by approx. NIS 314 million. The balance totaled approx. NIS 12.7 billion as of December 31, 2018, compared with approx. NIS 12.4 billion on December 31, 2017. The change mainly derives from investments in the segment's properties.

Change due to adjustment of the fair value of the segment's investment properties and investment properties under construction – The loss from such adjustment in the Report Period totaled approx. NIS 4 million, compared with a loss of approx. NIS 25 million in the same period last year. The properties are presented according to valuations prepared by an independent appraiser as of December 31, 2018.

Below is a summary of the business results of the retail centers and malls in Israel segment:

Summary of the Business Results of the Retail Centers and Malls in Israel Segment

| | For the Three Months Ended | | | For the Year Ended | | |
|---|---|---|---|---|---|---|
| | Rate of change | December 31, 2018 | December 31, 2017 | Rate of change | December 31, 2018 | December 31, 2017 |
| Revenues | 1% | 262 | 259 | - | 1,034 | 1,032 |
| NOI | (2%) | 206 | 210 | (1%) | 820 | 828 |

Figures are presented in millions of NIS.

The NOI decrease in the quarter chiefly results from the vacation of an income-producing area as part of the preparations for the excavation work at the Lodzia site. The NOI decrease in 2018 chiefly results from the vacation of an income-producing area as part of the preparations for the excavation work at the Lodzia site as well as from the effect of areas that were unoccupied during periods of tenant replacements in some of the malls, net of NOI increase resulting from the opening of the Rishonim Mall.

The following table presents the segment's NOI development:

Development of the NOI of the Retail Centers and Malls in Israel Segment

| | For the Three Months Ended | | For the Year Ended | |
|---|---|---|---|---|
| | 31.12.2018 | 31.12.2017 | 31.12.2018 | 31.12.2017 |
| For segment properties owned by the Company as of the beginning of the period | 206 | 208 | 780 | 789 |
| For properties purchased or construction of which was finished in 2017 | - | - | 40 | 31 |
| For properties operation of which was discontinued in 2017* | - | 2 | - | 8 |
| Total NOI from all properties | 206 | 210 | 820 | 828 |

*Vacation of space in the Lodzia construction site, as part of the preparations for excavation work
Figures are presented in millions of NIS.

Same-Property NOI in the retail centers and malls in Israel segment was primarily positively affected by a real increase in rent when renewing contracts for the various properties (due to the exercise of options by tenants and/or the execution of new contracts) and was negatively affected by areas that were unoccupied during periods of tenant replacements in some of the malls and by changes in operating expenses.

## 2.11. Office Segment

### 2.11.1.Description of the Office Segment

Israel's economy has continually grown in the past 15 years, and in 2018 the GDP increased by approx. 3.3%. Growth in 2018 encompassed all product components, export of good is expanded again, for the first time in two years, and inflation remained low. A low rate of unemployment was maintained, alongside the recorded growth, Israeli Governments initiated steps to encourage domestic employment.

Average occupancy rate in the office market continued to be high in 2018 throughout the country, with a slight increase in rent. Office spaces spanning approx. 200 thousand sqm were built in the past year in the center of Israel, of which approx. 130 thousand sqm are in Tel Aviv. Despite the construction momentum of the recent year, the office market maintains high occupancy rates throughout Israel, and the price level remains stable.[16]

Tel Aviv is Israel's business district, and presents the highest demand for leasable offices in the country. The Group has a number of leasable office properties in the city of Tel Aviv, the Azrieli Tel Aviv project, Azrieli Sarona and projects under development and construction, Azrieli Town and the expansion of the Azrieli Center. One of the changes in the office sector in recent years was the considerable expansion of international mega high-tech companies which launched or expanded their business in Israel, especially in the center.

The Company's portfolio of properties of leasable office space mostly consists of office towers classified as Class A properties, which are located mostly in CBDs, in proximity to major traffic arteries in the heart of the city. The location, quality and positioning of the office space enable the Company to maintain high occupancy rates, and over time increase the rent. The Company develops and builds office projects in significant scopes, which meet the international standards of employment centers in the world's largest cities, in all aspects pertaining to the management of the property and the quality thereof.

Furthermore, the Company has leasable office areas which are part of malls, in which small tenants offer services to the public (e.g. medical institutes, health funds and independent service providers). The combination of offices and retail increases customer traffic in these properties.

The Company's leasable office space properties are mostly characterized by the following:

- Positioning – among the Company's properties are projects which are considered to be leading and very significant in the field of leasable office spaces in Israel, and are an icon in Israeli landscape in general, and in Tel Aviv in particular, such as the Azrieli Tel Aviv Center and the Azrieli Sarona Tower.
- Location – the Company engages in the development of leasable office spaces and acts to locate and build its properties in this segment in areas which enjoy a high demand for offices. The Company's projects are mostly located in the heart of Israel's CBDs and in proximity to city centers and are characterized by convenient access by both private and public transportation. For example, the Company has several projects in Tel Aviv's northern CBD with both income-producing projects and projects under development and construction.
- Large floors – the Company's property portfolio includes a number of projects that can offer large floor spaces. These projects can meet the growing demand by large companies that are interested in creating one central site for employees, and their spread over a smaller number of floors. The planning of the Azrieli Sarona project and the Azrieli Holon center, for example, enables tenant to unite several sites which were previously spread across the country.

[16] From the yearbook of M.A.N Properties for 2017, of the CBRE Group.

- Building standard – the Group persistently applies high building standards to all of its properties, as expressed in the architectural design, the properties' functionality and the meticulous attention to high building qualities as well as to details such as new and fast elevators, advanced lighting and more. This is rooted in the long-term vision whereby the properties will be owned and managed by the Group for many years to come.
- Operational efficiency - The size of the Company's properties leads to operational efficiency which is expressed, *inter alia*, in the ability to implement technological and infrastructural improvements including the installation of complex communication networks and Leed Certificate which enable large multinational which require compliance with strict standardization to lease spaces at the Company's properties.
- Management – all of the Group's leasable office spaces are managed by management companies which are subsidiaries of the Company and are committed to high service standard.

Azrieli's office spaces in Israel are leased to some 650 different tenants. In each one of the Group's properties, there is a mix of tenants coming from various sectors. Some of the Company's office tenants are domestic or international mega-companies.

### 2.11.2.Performance of the Leasable Office and Other Space in Israel Segment and Changes in Value

The Group has 14 income-producing properties in this segment in Israel, with a total GLA of approx. 548,000 sqm.

Balance of the Group's investment properties in the leasable office and other space in Israel Segment – in 2018, the balance of investment property in this segment increased by approx. NIS 981 million. The balance totaled approx. NIS 10.4 billion as of December 31, 2018, compared with approx. NIS 9.5 billion on December 31, 2017. The change mainly derives from investments in the segment’s properties.

Change due to adjustment of the fair value of the segment’s investment properties and investment properties under construction – The profit from such adjustment in the Report Period totaled approx. NIS 167 million, compared with approx. NIS 630 million in the same period last year. The profit in the same period last year mostly derives from the revaluation of the Sarona office tower upon completion of construction. The properties are presented according to valuations prepared by an independent appraiser as of December 31, 2018.

Below is a summary of the business results of the leasable office and other space in Israel segment:

| Summary of the Business Results of the Leasable office and other space in Israel Segment | | | | | | |
|---|---|---|---|---|---|---|
| | For the Three Months Ended | | | For the Year Ended | | |
| | Rate of change | 31.12.2018 | 31.12.2017 | Rate of change | 31.12.2018 | 31.12.2017 |
| Revenues | 25% | 167 | 134 | 29% | 633 | 489 |
| NOI | 22% | 135 | 111 | 30% | 517 | 397 |

Figures are presented in millions of NIS.

The increase in revenues and in NOI chiefly results from the opening of the offices at Sarona and Rishonim in 2017.

The following table presents the segment's NOI development:

| Development of the NOI of the Leasable Office and Other Space in Israel Segment | For the Three Months Ended | | For the Year Ended | |
|---|---|---|---|---|
| | 31.12.2018 | 31.12.2017 | 31.12.2018 | 31.12.2017 |
| For segment properties owned by the Company as of the beginning of the period | 133 | 111 | 379 | 378 |
| For properties purchased or construction of which was finished in 2017 | - | - | 134 | 19 |
| For properties purchased or construction of which was finished in 2018 | 2 | - | 4 | - |
| Total NOI from all properties | 135 | 111 | 517 | 397 |

Figures are presented in millions of NIS.

Same-Property NOI in the leasable office and other space in Israel segment was primarily positively affected by a real increase in rent when renewing contracts for the various properties (due to the exercise of options by tenants and/or the execution of new contracts) and the continued lease-up of Azrieli Holon Center (in the current quarter was positively affected also from the continued lease-up of the offices in Sarona), and was adversely affected by interim period of tenant replacement and by changes in operating expenses.

## 2.12. Senior Housing Segment

### 2.12.1.Description of the Senior Housing Segment

Private senior housing in Israel most often appeals to senior Israelis from medium-high socio-economic background, offering housing services together with a multitude of complementary services aimed to enable residents to maintain an independent and satisfying lifestyle. The senior housing sector is growing as a result of the increase in life expectancy and the improved quality of life. We view constant growth in demand for housing solutions for seniors throughout the world. In Israel, this field is relatively underdeveloped, as compared to western countries in the world.

The Company considers the senior housing segment to be synergistic with its operations, using, *inter alia*, the years-long accumulated knowledge of the Group's managerial headquarters in respect of its operations in the field of income-producing properties. In all aspects pertaining to the senior housing segment, the Group benefits from its strengths in the location of lands, in purchase, development and efficient building and in the management of statutory processes including land use intensification. Economies of scale are also beneficial in terms of maintenance and operation of our existing senior homes. Finally, senior housing is also synergistic with retail: senior homes seek proximity to retail centers that will serve the residents of the complex.

The acquisition of land in Modi'in in 2014 marked the Group's entry into the senior housing segment, which was followed by the purchase of an existing senior home – Palace Tel Aviv, one of the most luxurious homes in Israel. Since the purchase of Palace Tel Aviv, the Group is acting under the brand "Palace" to continue the successful operation and to improve the three existing homes – Palace Tel Aviv, Palace Ra'anana (formerly "Ahuzat Bait") and Palace Modi'in (the construction of which was completed in Q3/2018), and to develop two additional projects, which are under various stages of development and construction in Lehavim and Rishon LeZion.

### 2.12.2.Performance of the Senior Housing Segment and Changes in Value

The Azrieli Group has 3 active senior homes with aboveground built-up areas of approx. 76 thousand sqm (excluding areas which are attributed to the LTC unit and to retail areas), which include approx. 800 senior housing units as well as 2 projects under development and construction in which approx. 600 residential units in a total area of approx. 59 thousand sqm (excluding areas which are attributed to the LTC unit and to retail areas). The Company is also promoting a zoning plan for additional rights, *inter alia*, for senior housing in the Azrieli Jerusalem mall.

Balance of the Group's segment properties in the senior housing segment – in 2018, the balance of the segment's properties in the senior housing segment increased by approx. NIS 356 million. This balance totaled approx. NIS 2.1 billion as of December 31, 2018, compared with approx. NIS 1.7 billion on December 31, 2017. The change mainly derives from investments in properties under construction.

Change due to adjustment of the fair value of the segment's investment properties and investment properties under construction – The profit from such adjustment in the Report Period totaled approx. NIS 103 million, compared with approx. NIS 81 million in the same period last year. The properties are presented according to valuations prepared by an independent appraiser as of December 31, 2018.

Below is a summary of the business results of the senior housing segment:

| Summary of the Business Results of the Senior Housing Segment | | | | | | |
|---|---|---|---|---|---|---|
| | For the Three Months Ended | | | For the Year Ended | | |
| | Rate of change | 31.12.2018 | 31.12.2017 | Rate of change | 31.12.2018 | 31.12.2017 |
| Revenues | 13% | 35 | 31 | 3% | 130 | 126 |
| NOI | (33%) | 6 | 9 | (5%) | 37 | 39 |

Figures are presented in millions of NIS.

The increase in revenues and the decrease in NOI in 2018 chiefly results from the opening of Palace Modi'in during 2018, as the gradual occupancy causes an operating loss that will be balanced as the home is occupied.

The following table presents the segment's NOI development:

| Development of the NOI of the Senior Housing Segment | | | | |
|---|---|---|---|---|
| | For the Three Months Ended | | For the Year Ended | |
| | 31.12.2018 | 31.12.2017 | 31.12.2018 | 31.12.2017 |
| For segment properties owned by the Company as of the beginning of the period | 9 | 9 | 39 | 39 |
| For properties purchased or construction of which was finished in 2018 | (3) | - | (2) | - |
| Total NOI from all properties | 6 | 9 | 37 | 39 |

Figures are presented in millions of NIS.

In 2018, the Same-Property NOI in the senior housing segment was primarily positively affected by the increased occupancy in the LTC and recovery units.

## 2.13. Income-Producing Properties in the U.S. Segment

### 2.13.1. Description of the Income-Producing Properties in the U.S. Segment

2001 marked the beginning of the Azrieli Group diversification's of its investments with income-producing real estate overseas. In recent years the Group has expanded its activity significantly through the acquisition of office buildings in Houston and in Austin, Texas.

The Azrieli Group aspires to increase the portfolio of income-producing properties overseas to approx. 15% of its total real estate properties. We focus on the purchase of existing, high-quality Class A properties, at a value that will not decrease approx. 40 million dollars. North America is still a major target market, however the Company will consider other western countries from time to time. Most of the Group's properties overseas are focused in strong metropolis areas with a population of at least 2 million people. The Group is focused on offices but is also considering other related fields such as logistics and data centers.

Some of the Group's properties overseas are held in partnership with local partners. However, a majority of the interests and control of all of the Group's overseas properties are held thereby. We manage the properties through local management companies, with control of the Azrieli Group.

Some of the Group's properties have recently undergone significant renovation of the buildings, including the public spaces, in order to maintain the positioning of the properties in the market.

The existing properties in the U.S. are financed separately from the corporate financing, through non-recourse dollar loans, other than irregular cases which are defined in the loan agreement and are considered common practice in the U.S. market.

On July 12, 2018, the Company, through an (indirectly) wholly-owned American corporation, closed the acquisition of an office building in Austin, Texas, U.S.A. (the "Property"), in consideration for approx. U.S. $100.4 million (including transaction costs), from a third party, in accordance with agreements for acquisition of the Property. The purchased Property is a 5-floor office building with a total area of approx. 23,214 sqm (approx. 249,870 sq ft) and an occupancy rate of approx. 100%. The Property also includes approx. 970 parking spaces, most of which are situated in a nearby 7-floor car park.

### 2.13.2.Performance of the Income-Producing Properties in the U.S. Segment and changes in Value

The Group has 8 income-producing properties in this segment, mostly in the U.S. with a total GLA of approx. 246 thousand sqm (on a consolidated basis) and approx. 236 thousand sqm (the Company's share) leased to some 250 tenants.[17]

Balance of the Group's investment properties in the income-producing properties in the U.S. segment – This balance totaled approx. NIS 2.6 billion as of December 31, 2018, compared with approx. NIS 2.0 billion on December 31, 2017. The change mainly derives from the purchase of the office building in Texas U.S.A., from investment in the existing properties and from the increase in the dollar exchange rate as of December 31, 2018 compared with December 31, 2017.

Change due to adjustment of the fair value of the segment's investment properties – The loss from such adjustment in the Report Period totaled approx. NIS 48 million, compared with a loss of approx. NIS 186 million in the same period last year. Most of the loss in the same period last year derived from investments that were and are expected to be made in properties as well as from the Company's provisions for the repair of the damage caused by Hurricane "Harvey" in some of the Company's properties in Houston, USA as well as from an increase in the cap rates in some of the properties (the Company recorded in 2017, other income of approx. NIS 64 million for other receivables insurance indemnity against the aforesaid damage).

Below is a summary of the business results of the income-producing properties in the U.S. segment:

Summary of the Business Results of the income-producing properties in the U.S. Segment – figures are presented in millions of U.S. Dollars.

| | For the Three Months Ended | | | For the Year Ended | | |
|---|---|---|---|---|---|---|
| | Rate of change | 31.12.2018 | 31.12.2017 | Rate of Change | 31.12.2018 | 31.12.2017 |
| Revenues | 27% | 19 | 15 | 21% | 74 | 61 |
| NOI | 22% | 11 | 9 | 21% | 41 | 34 |

[17] The "Company's share" – net of minority interests in certain companies.

| Summary of the Business Results of the income-producing properties in the U.S. Segment – figures are presented in millions of NIS. | | | | | | |
|---|---|---|---|---|---|---|
| | For the Three Months Ended | | | For the Year Ended | | |
| | Rate of change | 31.12.2018 | 31.12.2017 | Rate of Change | 31.12.2018 | 31.12.2017 |
| Revenues | 31% | 71 | 54 | 21% | 267 | 221 |
| NOI | 37% | 41 | 30 | 23% | 149 | 121 |

The increase in revenues and in NOI chiefly results from the fact that, at the end of 2017, the Group acquired the share of one of the partners in the projects One Riverway (33.33%) and Three Riverway (25%), such that its share in the ownership of such properties increased to 66.66% and 70%, respectively, from the purchase of the office building in Austin, Texas, U.S.A. and also from the lease-up of areas in existing properties.

The following table presents the segment's NOI Development:

| Development of the NOI of the income-producing properties in the U.S. Segment | | | | |
|---|---|---|---|---|
| | For the Three Months Ended | | For the Year Ended | |
| | 31.12.2018 | 31.12.2017 | 31.12.2018 | 31.12.2017 |
| For segment properties owned by the Company as of the beginning of the period | 34 | 30 | 138 | 121 |
| For properties purchased or construction of which was finished in 2017 | - | - | - | - |
| For properties purchased in 2018 | 7 | - | 11 | - |
| Total NOI from all properties | 41 | 30 | 149 | 121 |

Figures are presented in NIS in millions.

Same-Property NOI in the income-producing properties in the U.S. segment was affected by the aforesaid increase of the holding rate in One Riverway and Three Riverway (which increased the NOI by approx. NIS 3 million in the present quarter compared with the same quarter last year and by approx. NIS 11 million in the Report Period compared with the same period last year), and by an increase in occupancy in some of the properties.

# 3 | NON-REAL ESTATE BUSINESS

3 |

## 3.1. Granite Segment

The Azrieli Group, through Granite Hacarmel, holds 100% of the rights in Supergas Israeli Gas Distribution Company Ltd. ("Supergas"), which markets alternative energy sources; and 100% of the rights in G.E.S. Global Environmental Solutions Ltd. ("GES"), the business of which is water, wastewater, air, waste and industrial chemicals treatment.

A summary of the business results of the Granite segment follows:

**Summary of the Business Results of the Granite Segment**

| | For the Three Months Ended | | | For the Year Ended | | |
|---|---|---|---|---|---|---|
| | Rate of Change | 31.12.2018 | 31.12.2017 | Rate of Change | 31.12.2018 | 31.12.2017 |
| Net revenues | 15% | 196 | 170 | 2% | 720 | 705 |
| Segment profit | 43% | 33 | 23 | 13% | 117 | 104 |

Figures are presented in millions of NIS.

The increase in revenues in the Report Period chiefly derives from the results of Supergas, while the increase in the segment's profit in the Report Period derives from both Supergas and G.E.S.

Profit from discontinued operations (Sonol) – In July 2016, Granite closed the sale of its entire holding (100%) in Sonol. According to the provisions of IFRS 5, Sonol's results are presented as discontinued operations in the comparative figures to the income statement.

## 3.2. Additional Activities

### 3.2.1. Investments in Financial Corporations

The Group has holdings in the financial sector, with investments in Bank Leumi LeIsrael Ltd. and in Leumi Card Ltd.[18] A summary of changes in the investments in 2018 follows:

[18] The Company has also made negligible investments in investment funds and start-up companies, as specified in Section 14.2.3 of Chapter A herein.

| Changes in Investments in Financial Companies | Bank Leumi [1] | Leumi Card [2] | Total |
|---|---|---|---|
| Investment value in the financial statements as of December 31, 2017 | 1,132 | 536 | 1,668 |
| Divestment proceeds[3] | - | - | - |
| Total investment as of December 31, 2018[4] | 1,132 | 536 | 1,668 |
| Fair value of the investment as presented in the financial statements | 1,218 | 450 | 1,668 |
| Change in fair value during the Report Period | 86 | (86) | - |
| Dividend received in 2018[5] | 49 | 42 | 91 |

Figures are presented in millions of NIS.

(1) The fair value of the investment in Bank Leumi LeIsrael was determined according to the value of the share at the Tel Aviv Stock Exchange (TASE) as of December 31, 2018.

(2) The fair value of the investment in Leumi Card was determined according to the Company's share (20%) in the consideration set forth in the agreement for the sale of Leumi Card. For further details on the closing of the transaction for the sale of Leumi Card, see Section 1.3.9 of Chapter A herein. For the consideration received from the sale of Visa Europe, see Note 11B(2) to the financial statements.

(3) After the date of the financial statement, the Company sold the shares of Bank Leumi in the sum of approx. NIS 180 million.

(4) Before adjustment to changes in fair value during the Report Period

(5) With respect to the dividend declared by Bank Leumi and Leumi Card after the date of the financial statement, see Section 14.2 of Chapter A herein.

### 3.2.2. E-Commerce Platform – Azrieli.com

For details on the Group's e-commerce activity, see Section 14.1 of Chapter A herein.

4 |

## 4.1. Review of the Business Development Operations

### 4.1.1. Development of Income-Producing Properties

The Group's primary growth engine is expertise in development and unique architectural design of income-producing property project: malls, offices and senior housing. As of the date of the Report, the Company has ten projects at various development stages in Israel.

**Summary of Information about Properties Under Development**

| Name of Property | Use | Marketable Sqm[3] | Estimated Completion | Book Value of Project [1] | Cost Invested [2] | Estimated Construction Cost including Land[2] |
|---|---|---|---|---|---|---|
| Development Projects under Construction in the Short-Term | | | | | | |
| Azrieli Sarona Tel Aviv | Retail | 10,500 | 2019[11] | 308 | 331 | 335-345 |
| Palace Lehavim Senior Home | Senior housing | Phase A: 32,000 Phase B: 12,000 | Phase A: Q1/2020 Phase B: TBD | 139 | 131 | 400-410 |
| Azrieli Town Tel Aviv [4] | Retail, offices and residence | Offices 50,000 retail 4,000 residence 21,000 (210 residential units) | Retail and offices:2020 Residence: 2022 | 699 | 469 | 1,060-1,110 |
| HaManor Holon | Retail and offices | 28,000 | 2020 | 89 | 79 | 220-240 |
| Total | | 157,500 | | 1,235 | 1,010 | 2,015-2,105 |
| Development Projects in the Medium-Term | | | | | | |
| Expansion of Azrieli Tel Aviv Center (Spiral Tower) | Retail, offices, hotel and residence | 150,000[5] | 2025 | 756 | 444 | 2,300-2,500 |
| Modi'in land (Lot 21) | Retail, offices, residence and hotel | 20,000[8] | TBD | 123 | 130 | 350-380 |
| Senior housing land Rishon LeZion | Senior housing and retail | 28,750 [7] | TBD | 56 | 54 | 310-320 |
| Total | | 198,750 | | 935 | 628 | 2,960-3,200 |
| Total | | 356,250 | | 2,170 | 1,638 | 4,975-5,305 |
| Development Projects in Planning Stages | | | | | | |
| Azrieli Town Building E | Offices | 21,000 | TBD | [9] | [9] | TBD |
| Holon 3 – Holon Industrial Zone [6] | Retail and offices | 250,000 | TBD | 459 | 418 | TBD |
| Petach Tikva land | Offices and retail | 53,000[10] | TBD | 91 | 97 | TBD |
| Total | | 324,000 | | 550 | 515 | |
| Total | | 680,250 | | | | |

Cost and value figures are presented in millions of NIS.

All of the properties are held at a rate of 100% (excluding Azrieli Town Building E which does not include offices on an area of approx. 450 sqm and does not include a gas station and a convenient store next to it).

1. As of December 31, 2018.
2. Without capitalizations and tenant fit-outs, as of December 31, 2018.
3. With respect to the uses of senior housing and/or rental apartments the figure represents building rights in sqm.
4. The figures presented refer to the current zoning plan in respect of the land. As of the Report Release Date, the Group is promoting a zoning plan for additional office and residential rights. In May 2018, the Local Committee approved the deposit of a zoning plan for additional employment and hotel areas in the total scope of approx. 24 thousand sqm (gross) and in November 2018 the plan was deposited for objections. Furthermore, an aboveground permit has been received for the project.
5. In April 2018 a zoning plan was validated, which increases the building rights of the fourth tower and the expansion of the mall by approx. 80 thousand sqm, resulting in building rights of approx. 150 thousand sqm in total.
6. Includes additional land (marketable areas of approx. 27,000 sqm) originally purchased in the framework of an ILA tender, which was part of the Holon HaManor land. As part of parcel consolidation, building rights of approx. 30,000 sqm were added to the lot (such that the total building rights in the consolidated lot sum up to approx. 250,000 sqm).
7. The data presented relate to the existing zoning plan on the land. The Company is in the process of increasing the building rights in the project by approx. 33,000 sqm (above and below ground).
8. The Group is in the process of increasing the building rights in the project to 28,000 sqm.
9. The building rights were purchased in the framework of the purchase of the income-producing property in May 2018.
10. The data presented relate to the existing zoning plan on the land. The Group is in the process of increasing the building rights in the project to approx. 150,000 sqm.
11. An occupancy form was received in January 2019 for part of the western façade of the mall.

During the Report Period, the Company proceeded with the work of development and construction of its aforesaid properties and with its efforts for the obtainment of the approvals required for the purpose of their continued development on schedule and without significant delays. Furthermore, the Group is negotiating on and is engaging in contracts for the lease of areas under construction. For further details, see Section 7.7-7.8 of Chapter A herein.

Description of Properties under Development

Azrieli Sarona, Tel Aviv – The land, area of which is approx. 9,400 sqm, was purchased in May 2011 and construction commenced in May 2012. Construction of the office tower, with a GLA of approx. 119,000 sqm, was completed in Q2/2017. The construction of the mall, which is located at the base of the office tower, is expected to end in the course of 2019. A certificate of occupancy for part of the western façade of the mall was received in January 2019. The office tower is fully leased-up.

"Palace Lehavim" Senior Home – The land, area of which is approx. 28,300 sqm, was purchased in December 2014 and construction commenced in August 2016. The plan is to build a retirement village to high and innovative standards. The project, on a built area of approx. 44,000 sqm (principal and service), is expected to comprise approx. 350 residential units and an LTC unit, with related facilities, such as a swimming pool, sports center and retail areas of up to approx. 1,500 sqm. In May 2018, an application for a changes permit for the project was approved, for the addition of another LTC unit, and the permit was received in October 2018.

Azrieli Town, Tel Aviv – The land, area of which is approx. 10,000 sqm, was purchased in October 2012 and construction commenced in September 2016. The project is expected to consist of a retail spaces of approx. 4,000 sqm and two towers: an office tower with a GLA of approx. 50,000 sqm and a residential tower consisting of approx. 210 apartments for lease. The project is located in proximity to the train stations in central Tel Aviv and to the light rail station in the future, and the Emek Bracha Bridge, which is planned to be built in the area, will connect the eastern side of the city with the city center through the project. The Group is promoting a change of the zoning plan to increase the building rights in the complex. In November 2018, a zoning plan was published for deposit for the addition of commercial and hotel areas in the total scope of approx. 24,000 sqm (gross). In May 2018, an aboveground permit was received for the project. As of the Report Release Date, the

Group has signed lease contracts in respect of approx. 41,000 sqm of the project's office space, which represent approx. 82% of its leasable office space.

HaManor, Holon – Land, which is situated near the Azrieli Holon Center and is around 6,200 sqm, was purchased in February 2015. Construction of the project began in August 2017. The plan is to build approx. 28,000 sqm of office and retail. In September 2018, an above-ground permit was received for the project. Completion of the project is scheduled for 2020. A contract was signed with Bezeq The Israel Telecommunication Corp. Limited in respect of approx. 70% of the project's leasable areas.

Expansion of Azrieli Tel Aviv Center (Spiral Tower) – The land, area of which is approx. 8,400 sqm, was purchased in May 2013 and construction commenced in September 2016. The land, which is adjacent to the Azrieli Tel Aviv Center will enable the construction of the fourth tower and the expansion of Azrieli Tel Aviv mall. In April 2018, a zoning plan was validated with an urban-mixed designation, which allows uses of retail, offices, hotels, residence and senior housing with aboveground building rights of approx. 147,260 sqm (gross), and, in addition, approx. 3,000 sqm of underground main retail space. In the framework of the committee's decision, the Company has undertaken to allocate from the aforesaid rights in the project up to two public floors to the Municipality of Tel Aviv-Jaffa and has also undertaken to perform various tasks in the vicinity of the project, including in the Azrieli Center. The Company intends to construct retail space that will serve to expand the existing mall and a multi-story tower, the Spiral Tower. As of the Report Date, the Company is performing excavation and shoring work on the land.

Land in Modi'in (Lot 21) – On January 11, 2018, the Group won a tender held by the Israel Land Authority for the purchase of a leasehold in a lot located in the CBD of Modi'in-Maccabim-Re'ut (close to the Azrieli Modi'in Mall), in an area of approx. 5,300 sqm, designated for the construction of 80 residential units, 50 hotel rooms, offices and retail space, in consideration for approx. NIS 101.5 million. The Company is acting to increase the building rights in the lot to 28,000 sqm and its connection with the existing project. For further details, see the Company's immediate report of January 11, 2018 (Ref.: 2018-01-004960), which is incorporated herein by reference.

"Palace Rishon LeZion" Senior Home – The land, area of which is approx. 3,400 sqm, located at HaRakafot Neighborhood in East Rishon LeZion, was purchased in March 2016 through a tender held by the ILA for the purchase of a leasehold in the land. The project is in planning stages. The Company intends to build on the land a senior home which is planned to consist of approx. 250 residential units and approx. 3,000 sqm of retail space. In April 2018, the recommendation of the Local Committee was received for the deposit of a zoning plan for additional aboveground building rights and was referred for a discussion at the District Committee. In November 2018, the District Committee decided to deposit the plan on conditions, and the Company promotes the publication of the plan for deposit.

Azrieli Town E – On May 14, 2018, the Company closed a transaction for the purchase of rights to land located on Menachem Begin Road, Tel Aviv, holding a 4-floor building over a commercial ground floor, in the total area of approx. 5,500 sqm and underground floors mostly leased for office purposes. The property includes unused building rights under the zoning plan that applies to the land, in the total scope of approx. 21,000 sqm above-ground, as well as additional rights.

Holon 3 - Holon Industrial Zone – The land is in the area of approx. 57,500 sqm., and its purchase was closed in April 2016. Construction commenced in March 2018 and in June 2018, excavation and shoring work commenced in the project. In October 2018, a building permit was received for the car park basements in the project. The land is located in proximity to the Azrieli Holon Center, on which it is planned to build a very large employment and commerce project of leasable office space and a family-friendly entertainment and shopping complex. In the context of parcel consolidation, building rights of approx. 30,000 sqm were added in the lot (such that the building rights in the consolidated lot total approx. 250,000 sqm). The project is in proximity to central traffic arteries.

Land in Petach Tikva – The land, which was purchased in November 2017, of an area of 19,000 sqm, is situated in the eastern part of the Kiryat Aryeh Industrial Zone in Petach Tikva, near an existing office project owned by the Group. The land includes building rights for around 53,000 sqm as well as parking basements. As of the

Report Release Date, the Company is promoting a zoning plan for additional rights, based on a zoning plan which is being promoted by the Municipality in the area, such that its total rights will amount to approx. 150 thousand sqm. The Group intends to build an office project on the land. For further details, see the Company's immediate reports of September 18, 2017 and November 9, 2017 (Ref.: 2017-01-093630 and 2017-01-098386, respectively) which are incorporated herein by reference.

*The Company's estimations in Section 4.1.1 herein, with regard to, inter alia, the investment in and expected costs of properties under construction, the financing manner of the projects, the construction completion dates, the receipt of various regulatory approvals which are required for the promotion of the projects under construction or the outcome of administrative and legal proceedings are forward looking information as per the definition thereof in the Securities Law, which is based on the Company's subjective estimations as of the date of the Report, and there is no certainty regarding their materialization, in whole or in part, or they may materialize in ways which may differ significantly, inter alia for reasons which are beyond the Company's control, including changes in the market conditions, changes in the Company's plans, the time that will take to have the zoning plans approved for execution and the prices of construction input.*

For details on the projects under construction, See Section 7.7 of Chapter A of this Report.

The Company's management is acting to continue leading the income-producing real estate market, *inter alia* through the purchase of land reserves, the expansion of existing properties and the purchase of additional similar properties as aforesaid, in order to bring to a further increase in the Company's future operating cash flow, insofar as the Company's board of directors shall so deem fit, and to further consider the development of related and/or synergistic segments.

# DEVELOPMENT PIPELINE*

* For further details, including in connection with the scope of the building rights in the development pipeline, see the footnotes in the development pipeline table above.

## EXPANSION OF AZRIELI TEL AVIV CENTER

| | |
|---|---|
| Use | Retail, offices and residence |
| GLA | 150,000 sqm |
| Estimated completion | 2025 |
| Status | Under Construction |

## AZRIELI HOLON 3

| | |
|---|---|
| Use | Retail and offices |
| GLA | 250,000 sqm |
| Estimated completion | TBD |
| Status | Under Construction |

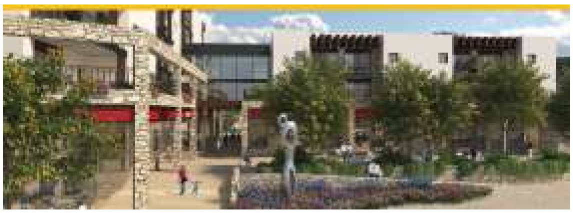
## PALACE RISHON LEZION SENIOR HOME

| | |
|---|---|
| Building rights | 28,750 sqm |
| No. of residential units | 250 |
| Estimated completion | TBD |
| Status | In planning |

## MODI'IN LAND (LOT 21)

| | |
|---|---|
| Use | Retail, offices, hotel and residences |
| Building rights | 20,000 sqm |
| Estimated completion | TBD |
| Status | In planning |

## PALACE LEHAVIM SENIOR HOME

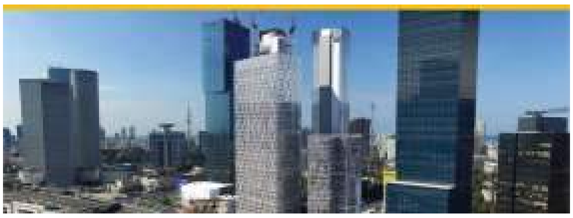


| | |
|---|---|
| Building rights | 44,000 sqm |
| No. of residential units | 350 |
| Estimated completion | Phase A: 2020 \| Phase B: TBD |
| Status | Under Construction |

## AZRIELI SARONA (RETAIL)

| | |
|---|---|
| Use | Retail |
| GLA | 10,500 sqm |
| Estimated completion | 2019 |
| Status | Under Construction |

## AZRIELI TOWN



| | |
|---|---|
| Use | Retail, offices and residence |
| GLA | 75,000 sqm |
| Estimated completion | Offices and retail: 2020 \| Residence: 2022 |
| Status | Under Construction |

## AZRIELI HOLON HAMANOR

| | |
|---|---|
| Use | Retail and offices |
| GLA | 28,000 sqm |
| Estimated completion | 2020 |
| Status | Under Construction |

## PETACH TIKVA LAND

| | |
|---|---|
| Use | Offices and retail |
| GLA | 53,000 sqm |
| Estimated completion | TBD |
| Status | In planning |

## AZRIELI TOWN BUILDING E

| | |
|---|---|
| Use | Offices |
| GLA | 21,000 sqm |
| Estimated completion | TBD |
| Status | In planning |

### 4.1.2. Betterment of income-producing properties

Another growth engine of the Company is the betterment of its existing properties. The Company also examines, from time to time, options to promote zoning plans for additional building rights in its properties.

As of the Report Release Date, the Company is acting to improve its properties, as follows:

Azrieli Akko Mall – a further hearing in the Local Committee was held in September 2018, on the application for approval of the permit for the addition of parking and office floors, the application was approved and the Company is working towards the fulfillment of the conditions for receipt of the permit.

Azrieli Jerusalem mall – The zoning plan for expansion of the mall, senior housing and office space was discussed at the Local Planning and Building Committee and its recommendation was received for deposit to the district committee. In July 2018, the Jerusalem District Planning and Building Committee approved the Company's application for the deposit of a plan for expansion of the areas of Azrieli Jerusalem mall by approx. 100 thousand sqm gross, above-ground, which include retail, employment and senior housing areas and a building to be built for the Jerusalem municipality, and the Company is acting to publish the plan for deposit.

Azrieli Givatayim Mall – the Company completed the renovation of the mall's fast-food court.

Azrieli Tel Aviv – the Company completed the renovation of the fast-food court in the mall and continues the upgrade of the office elevators, and is further acting to renovate the public areas of the project.

Herzliya Business Park – in June 2018, the Local Committee approved a plan for deposit for the addition of two office floors, and for the addition of retail spaces in the project. The deposit is subject to the approval of the District Committee.

Palace Ra'anana Senior Home – in June 2018, the Local Committee discussed the objections submitted for the plan and approved the plan for validation, subject to various amendments. In November 2018 the Company notified the Local Committee of the cessation of the promotion of the plan.

Azrieli Rishonim –a zoning plan for additional office spaces at the office tower of the project, was recommended for deposit by the Local Committee and was referred to a hearing in the District Committee.

### 4.1.3. Identification and acquisition of properties in the Company's operating segments

One of the Company's main growth engines is its know-how, expertise and experience in the identification and acquisition of attractive properties that will yield a high return, with high demand and an improvement potential. The Company estimates that the success factors in the acquisition of such properties in its operating segment are, *inter alia*, the identification of worthwhile transactions and of opportunities in the market, positive goodwill together with business positioning and financial solidity which enable the acquisition of income-producing properties and a fast response to attractive business opportunities.

As previously reported, the Group examines, from time to time, the expansion of its business including entry to related real estate sectors, through, *inter alia*, the identification and acquisition of income-producing properties as aforesaid.

# 5 | FINANCING OF THE BUSINESS

5 |

## 5.1. Leverage Ratio of the Group

The following table presents a summary of balance sheet figures out of the consolidated financial statements:

| Summary of Balance Sheet Figures out of the Consolidated Statements | | |
|---|---|---|
| | 31.12.2018 | 31.12.2017 |
| Current assets | 1,885 | 1,940 |
| Non-current assets | 30,010 | 28,203 |
| Current liabilities | 3,092 | 2,829 |
| Non-current liabilities | 11,682 | 10,993 |
| Equity attributable to the Company's shareholders | 17,077 | 16,281 |
| Equity attributable to the Company's shareholders out of total assets (percentage) | 54% | 54% |
| Net debt to assets (in %) | 29% | 27% |

Figures are presented in millions of NIS, unless otherwise noted.

The Group funds its business operations primarily out of its equity, cash and cash equivalents and by means of non-bank credit (mainly bonds and loans from institutional bodies), bank credit (short-term and long-term) and commercial paper. During the Report Period, the Company issued Bonds to the public through the expansion of Series D bonds and after the Report Period, through the issuance of new Series E-F bonds. The issues were made based on a shelf prospectus.

The Group's financial soundness, which is characterized by a low leverage ratio and considerable unencumbered assets, affords the Group available sources for the obtainment of financing on convenient terms.[19] The Group's leverage ratio is low, compared to many of its major competitors. The Group's low leverage ratio, joined with the Company's extensive initiatives in the real estate sector, provide flexibility also at times of crises.

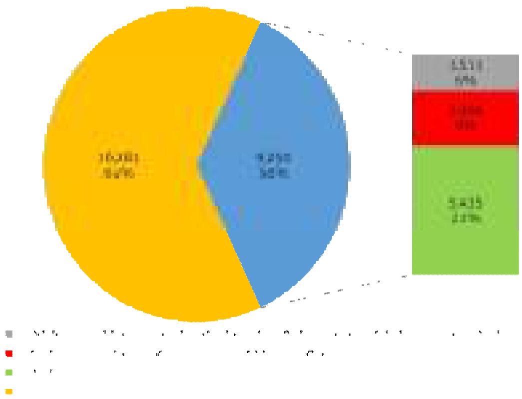
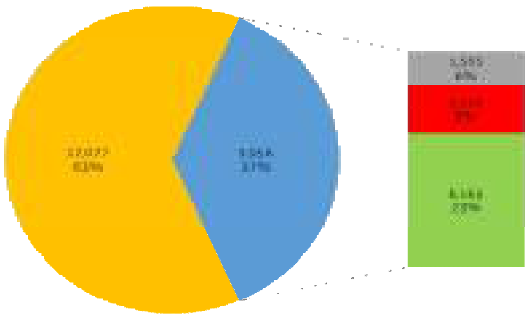
## 5.2. Composition of Financing Sources

The Group has three principal debt channels: bank debt, private loans from institutional bodies or public bonds. The Group currently enjoys very high accessibility to each of these financing channels.

The following chart presents a breakdown of the rate of borrowed capital in the Company's total capital, as well as a breakdown thereof by type:

[19] For further details, see Section 19 of Chapter A herein.

## Composition of Capital and Breakdown of Debt of the Group

| December 31, 2017 | December 31, 2018 |
|---|---|
|  |  |

Figures are presented in millions of NIS and as a percentage out of total assets.

The increase in the total debt, in the sum of approx. NIS 706 million in the Report Period mainly stems from the issue of bonds in Q1/2018 net of current maturities of loans and bonds. As of the date of the Report, the Group, on a consolidated basis, has a working capital deficit of approx. NIS 1.2 billion (approx. NIS 0.5 billion in the separate statement), which derives, *inter alia*, from the Company's management's decision, at this stage, to fund its business also by means of short-term credit, in view of the business opportunity arising from the low interest rates on credit of this type.

The Group estimates that if it decides at any time to convert such credit into long-term credit, it will be able to do so in view of its financial soundness and/or the scope of its unencumbered assets. Therefore, in its meeting of March 19, 2019, the Company's board of directors, having examined the Group's cash flow and financing sources, determined that such working capital deficit does not affect its ability to timely repay its liabilities.

*The Group's estimations mentioned in this Section 5.2 herein in relation to its liquidity and the availability of its financing sources, particularly as pertains to the possibility of converting the short-term debt into long-term debt, are forward-looking information within the definition of this term in the Securities Law, which is based on the Company's assessments as to market developments, inflation levels and projected cash flows and on the conditions and possibilities of obtaining credit on the date of the Report. Such estimations may not materialize, in whole or in part, or may materialize in a manner that materially differs from the Company's estimations. The primary factors that may affect the above are: changes in the capital market affecting the conditions and possibilities of obtaining credit, changes in the Company's plans, including the use of future available liquid balances in order to seize business opportunities, changes in the advantageousness of the holding of various investment channels or the advantageousness of use of various financing channels, deterioration of the Israeli or U.S. economy and decline into severe recession, and the Company or any of the Group's companies encountering financing or other difficulties, in a manner affecting the Company's cash flow.*

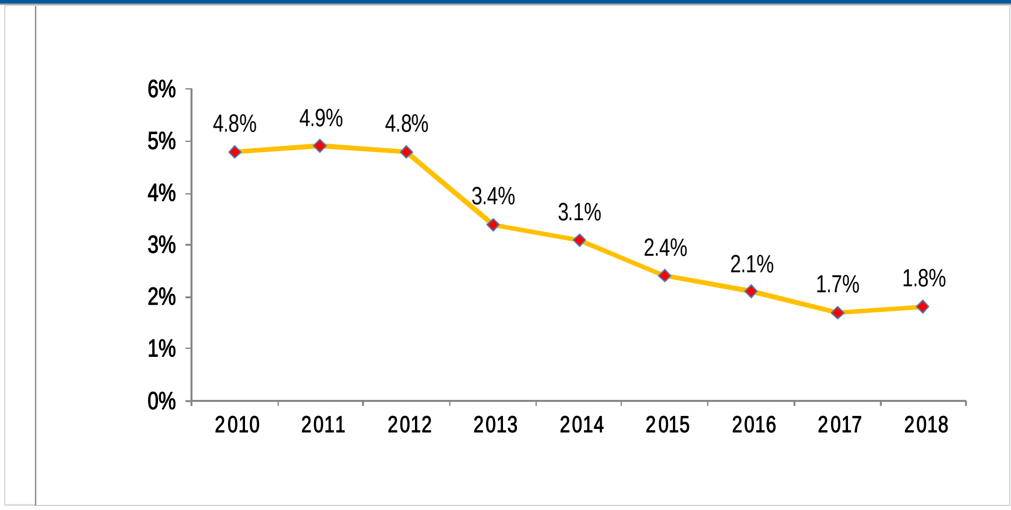
Regarding collateral and liens that were provided against the debt, as well as financial covenants with respect to the debt, see Note 19 and Note 30 to the financial statements in Chapter C of this Report.

## 5.3. Financing Transactions during the Report Period and until the Report Release Date

During the Report Period and in the course of Q1/2019, the Company raised debt at low interest rates, which are typical in the present market conditions, whilst maintaining the Company's high credit rating and extending the loans' debt duration.

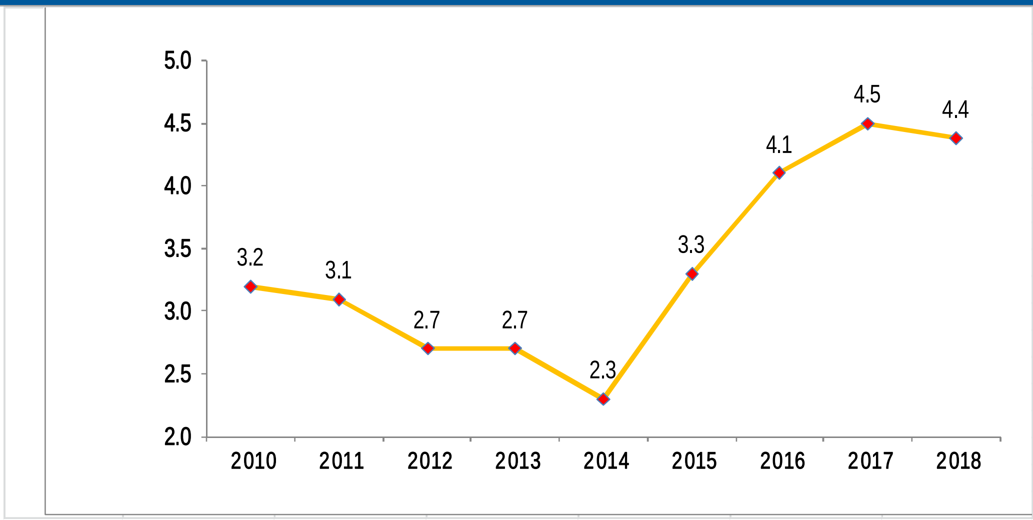
The Company acted during the Report Period and until the Report Release Date to raise debt through the expansion of Series D bonds of the Company in the scope of approx. NIS 1.4 billion, with a duration of approx. 6 years and weighted index-linked interest of approx. 0.94% and after the Report Period, raised debt through the issue of Series E and F bonds in the scope of approx. NIS 1.5 billion, with a duration of approx. 7.5 years and weighted index-linked interest of approx. 1.9% . For details on the debt raising see Section 19 of Chapter A of this Report.

Reduction of Average Interest over the Years




◆ Interest rate as of the end of the year

Extension of the Average Duration of Debt




◆ Duration as of the end of the year

* After the Report Period, in January 2019, the Company issued two bond series (Bond Series E and F), as described in Section 1.2.3.10 above, following which the debt duration increased to 4.8 years.

## 5.4. Rating

The Company's credit rating is high and reflects its financial strength, the quality of its assets and its low leverage ratio. As of the end of 2018, the Group's bonds are rated, as of the date of the Report, AA+/Stable/ilA-1+ by Ma'alot and Aa1 by Midroog.

In recent years, Azrieli has maintained a stable credit rating, which has even been upgraded:

- In November 2015, Moody's Midroog credit rating agency upgraded Azrieli's credit rating from Aa2 to Aa1. The rating outlook is stable.
- In January 2015, S&P Ma'alot upgraded Azrieli's credit rating from AA to AA+. The rating outlook is stable.

Various parameters that have had an effect on the Company's high rating are the low leverage ratio, the high debt repayment capacity (debt to FFO ratio), a broad dispersal of properties and tenants, various and diverse operating segments of income-producing properties, excellent locations of the properties, the considerable scope of unencumbered assets and focusing on the Company's core operations – income-producing properties.

## 5.5. Liabilities and Financing

Below is a summary of the Group's financial liabilities (excluding Granite Hacarmel and Azrieli E-Commerce):

| Breakdown of Financial Liabilities | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Fixed Interest | | | Variable Interest | | Total | | Total |
| | Index-linked | USD-linked | Unlinked | GBP-linked | Unlinked | Fixed Interest | Variable Interest | |
| Short-term loans | - | - | - | 20 | 436 | - | 456 | 456 |
| Long-term loans | 7,625 | 1,461 | - | - | 27 | 9,086 | 27 | 9,113 |
| Total | 7,625 | 1,461 | - | 20 | 463 | 9,086 | 483 | 9,569 |

Figures are presented in millions of NIS as of December 31, 2018.

As of December 31, 2018, short-term loans represented approx. 5% of the Group's total financial liabilities (excluding Granite Hacarmel and Azrieli E-Commerce). The Company's management estimates that this rate is low and conservative in view of the low leverage ratio and the total unencumbered assets as specified below.

The Company's policy regarding the financing of its business, besides the positive and stable cash flow from current operations and current assets, is implemented primarily by taking long-term index-linked fixed-interest loans, in order to minimize market risks resulting from changes in the market interest rates and to counteract the market risk resulting from changes in the Consumer Price Index (CPI), while taking advantage of the fact that the Company's revenues are, for the most part, index-linked. However, in view of the low interest rates on short-term variable-interest loans, the Company's have decided to finance its operations also by means of short-term loans as specified above.

## 5.6. Designated Disclosure to Bondholders (of Series B-D)

For details with respect to designated disclosure to the holders of the Company’s Series B-D Bonds, see Annex C to this chapter.

## 5.7. Maturities of the Group’s Financial Liabilities

The following table presents the maturity dates and amounts of financial liabilities (excluding Granite Hacarmel and Azrieli E-Commerce):

| Forecast of Maturities of Financial Liabilities | | | |
|---|---|---|---|
| Year | Principal | Interest | Total |
| 1 | 1,492 | 171 | 1,663 |
| 2 | 981 | 148 | 1,129 |
| 3 | 1,381 | 111 | 1,492 |
| 4 | 748 | 92 | 840 |
| 5 forth | 4,967 | 384 | 5,351 |
| Total | 9,569 | 906 | 10,475 |

Figures are presented in millions of NIS as of December 31, 2018.

In the past year, the sources for the funding of the Group's financial liabilities were chiefly the following:

- Positive cash flow from current operations, which totaled approx. NIS 1,266 million in the year ended December 31, 2018, compared with NIS approx. 1,219 million in the same period last year.
- Liquid assets and unencumbered assets.
- The Group has mortgaged income-producing properties, the fair value of which significantly exceeds the loan undertaken therefor.
- Refinancing of debts in the capital market and/or institutional bodies and/or banks.

## 5.8. Unencumbered Assets Available to Serve as Collateral against the Receipt of Credit

As of December 31, 2018, the aggregate amount of liquid assets (cash and cash equivalents and short-term investments and deposits) held by the Group amounted to approx. NIS 763 million. The Company deems its liquid assets, the considerable cash flow from its current operations and its unencumbered assets (in the total value of NIS approx. 22 billion, in addition to the aforesaid approx. NIS 0.8 billion) essential to its financial soundness, its high financial flexibility due to its lack of dependence on the availability of external sources both in terms of debt repayment and in terms of the ability to seize investment opportunities at various times.[20] As pertains to additional possible liquid sources, the Group estimates that it has the ability to obtain financing on convenient terms in the prevailing economic conditions.

**Unencumbered Assets Available to Serve as Collateral against the Receipt of Credit**

| Assets | Value of Assets as of 31.12.2018 |
|---|---|
| Real estate of the retail centers and malls in Israel segment | 10,618 |
| Real estate of the leasable office and other space in Israel segment | 8,888 |
| Other real estate (chiefly senior housing) | 251 |
| The Company's holdings in Azrieli E-Commerce | 51 |
| The Company's holdings in Leumi Card | 450 |
| The Company's holdings in Granite Hacarmel | 587 |
| The Company's holdings in Bank Leumi | 1,218 |
| Total | 22,063 |

Figures are presented as presented in the financial statements and in millions of NIS.
In addition, the Group holds mortgaged income-producing properties, the fair value of which exceeds the amount of the loan undertaken therefor.

*The Group's estimations mentioned in Section 5.8 herein in connection with the Company's ability to obtain financing on convenient terms in the currently prevailing economic conditions, are forward-looking information, as defined in the Securities Law, which is based on the Company's estimations as to the economic conditions and the liquidity level as of the date of release of this report. Such estimations may not materialize, in whole or in part, or may materialize in a manner that materially differs from the Company's estimations. The primary factors that may affect the above are: changes in the capital market affecting the conditions and possibilities of obtaining financing, changes in the Company's plans, including use of future available liquid balances in order to seize business opportunities, changes in the advantageousness of the holding of various investment channels or the advantageousness of use of various financing channels, deterioration of the Israeli or U.S. economy and decline into severe recession, in a manner which affects the Company's ability to obtain financing on convenient terms.*

[20] For details with respect to additional matters related to the Group's financing activities, see Section 19 of Chapter A herein.

## 5.9. Financial Position

| Financial Position, Liquidity and Financing Sources | | |
|---|---|---|
| Item | 31.12.2018 | 31.12.2017 |
| Total assets [1] | 31,895 | 30,143 |
| Current assets [2] | 1,885 | 1,940 |
| Investment properties [3] | 27,452 | 25,206 |
| Short-term credit[4] | 1,565 | 1,511 |
| Loans from banks and other credit providers [5] | 2,226 | 2,304 |
| Net bonds [6] | 6,165 | 5,435 |
| Equity [7] | 17,121 | 16,321 |

Figures are presented in millions of NIS.

(1) Increase chiefly results from an increase in investment properties and in investment properties under construction as a result of the progress of the investments in projects under construction and in the income-producing properties and from purchases of new properties, net of a decrease in cash and deposits and short-term investments.

(2) Decrease chiefly results from the decrease in balances of cash and deposits and short-term investments, net of classification of the investment in Leumi card as an asset held for sale.

(3) Increase results from the progress of the investments in projects under construction and in income-producing properties, from the acquisitions of the office building in Texas, U.S.A., the land in Modi'in and rights in the land on Menachem Begin Road in Tel Aviv, from an increase in the fair value due to appraisals of the Company's assets and an increase in the Dollar exchange rate.

(4) The increase derives mainly from an increase in the current maturities of the bonds due to the issue of bonds in Q/1 2018 net of repayment of short-term credit.

(5) Decrease chiefly results from current repayments, offset by a loan taken for the acquisition of the office building in Texas, U.S.A.

(6) Increase results from the issue of bonds at the end of Q1/2018, net of current maturities.

(7) Increase chiefly results from the comprehensive income net of a dividend distribution.

# 6 | BUSINESS RESULTS AT A GLANCE

6 |

## 6.1. Summary of Business Results

The following table presents the consolidated net profit of the Azrieli Group:

| Year | 2018 | 2017 | 2016 |
|---|---|---|---|
| Net profit for the period attributable to the shareholders | 1,218 | 1,456 | 1,810 |
| Net profit attributable to the shareholders and to non-controlling interests | 1,219 | 1,448 | 1,808 |
| Basic earnings per share (NIS) | 10.04 | 12.01 | 14.93 |
| Basic earnings per share from continuing operations (NIS) | 10.06 | 12.01 | 15.00 |
| Comprehensive income to shareholders and non-controlling interests | 1,325 | 1,476 | 1,893 |

Net profit in the Report Period totaled NIS 1,219 million, compared with NIS 1,448 million in the same period last year. The profit in the Report Period was affected by a profit from fair value adjustments of investment property in the sum of NIS 218 million, which is lower than the same period last year (the profit in the same period last year, totaling NIS 500 million, included revaluation after completion of the construction of the office tower in Sarona), by an increase in the net financing expenses in the sum of NIS 151 million (mostly due to profit from the sale of Bank Leumi shares, that was recorded last year), and by a decrease in other income, net, of NIS 36 million, offset by an increase in NOI from the real estate activity of NIS 138 million and a decrease in the tax expense, mainly due to the aforesaid in the sum of NIS 115 million.

## 6.2. Profit Quality

The Group’s net profit mainly consists of and is affected by the following components:

- Profit from the income-producing real estate business – Retail centers and malls in Israel, leasable office and other space in Israel, income-producing properties in the U.S. and senior housing;
- Changes in the fair value of the Group’s investment properties;
- The Group’s share in the income of the Granite Hacarmel segment;
- The Company’s HQ operation, which includes net financing expenses as well as administrative and general and marketing expenses;
- Deferred and current tax expenses;
- The Company’s share in the results of Azrieli E-Commerce.

Income from the real estate business is primarily affected by the rent revenues from the various properties, which are mainly affected by supply and demand in the rental market.

The Group’s income may be subject to sharp fluctuations between reporting periods, chiefly due to changes in the value of the income-producing real estate as aforesaid, which is affected, *inter alia*, by changes in the cap rates and by a change in the amount of the revenues resulting from changes in market conditions and/or a rise of the CPI. Furthermore, the Group's financing expenses are affected, *inter alia*, by changes in variable interest rates and changes in the CPI.

The Group examines the fair value of the investment properties in Israel at least once every six months and whenever there are indications of material changes in value. The determination of fair value is mainly based on valuations that are mostly prepared by appraisers who are not dependent on the Company. Fair value is measured based on discounted cash flows based on signed contracts and market rent for vacant space as of the date of examination, supported by their comparison to renewals in locations similar to the property's location close to the date of the valuation, as well as use of cap rates that are examined, *inter alia*, by analyzing comparable transactions close to the date of the valuation. The Group considers the need for an update of the value of investment properties every quarter, by examining macroeconomic changes, changes in the properties' environment and in the revenues generated therefrom, and also holds discussions with an independent real estate appraiser for examination of changes in the cap rates. Furthermore, for investment properties under construction, the costs actually invested in the period, the up-to-date forecast of costs for completion and lease contracts signed in the course of the period are taken into account. Insofar as the Company's Management estimates that material changes occurred in the value of the properties, as defined in the Group's procedures, up-to-date valuations of the relevant properties are prepared by the Company or by an appraiser.

Changes in the assumptions used by external experts and/or changes in the estimations of the Group's management, which relies on its accumulated experience, may lead to a change in the fair value recorded in the income statement, thereby affecting the Group's financial position and results of operations. For further details, see Note 34 to the financial statements.

For details with respect to the fair value of investment properties by operating segment, see Section 7.4 of Chapter A herein. Also see Notes 13 and 36 to the attached financial statements.

## 6.3. Comprehensive Income

The Group's capital and comprehensive income are also affected by various capital reserves, chiefly by capital reserves in respect of adjustment to the fair value of investments in equity instruments designated at fair value through other comprehensive income and by reserves for translation differences from foreign operations. The difference between the comprehensive income and the net profit as presented in Section 6.1 herein, derives chiefly from profit from translation differences from foreign operations of NIS 95 million and an increase in the fair value of financial assets net of tax in the amount of approx. NIS 11 million.

## 6.4. Results of Operations

The following table presents the marketing, general and administrative expenses, other revenues, financing expenses and income taxes in Y2018, compared with Y2017, and in Q4/2018 compared with Q4/2017:

| Results of Operations | | | | |
|---|---|---|---|---|
| | Q/4 2018 | Q/4 2017 | 2018 | 2017 |
| Marketing, general and administrative expenses(1) | 92 | 88 | 323 | 306 |
| Net other revenues (2) | 22 | 71 | 88 | 124 |
| Net financing expenses (3) | 66 | 44 | 241 | 90 |
| Income taxes expenses (4) | 115 | 69 | 293 | 408 |

Figures are presented in millions of NIS.

(1) The increase in expenses in Y2018, compared with the same period last year, mainly derives from an increase in marketing expenses, an increase in expenses due to doubtful debts and in payroll expenses, mainly due to a one-time provision for adjustment.

The increase in expenses in Q4/2018 compared with the same quarter last year mainly derives from an increase in marketing expenses.

(2) Net other revenues in 2018 chiefly result from dividends from Bank Leumi and Leumi Card (in 2017, from dividends from Bank

Leumi and from Leumi Card and from profit from the sale of Visa Europe and in Q4/2017 also due to amounts receivable from the insurance company as indemnification for the damage of the storm that had hit the Company's properties in Houston, Texas)).

(3) The increase in net financing expenses in 2018 mainly stems from a profit from the sale of the shares of Bank Leumi that was recorded in the same period last year and did not happen in the Report Period, and from an increase in the linkage expenses on loans, bonds and senior housing residents' deposits, as a result of an increase of approx. 1.2% in the rate of the known index during the Report Period, compared with an increase of approx. 0.3% in the same period last year. The rise in net financing expenses in Q4/2018 compared to the same quarter last year, mainly derives from income tax interest expenses due to the assessment arrangement and from a loss from the revaluation of financial assets that were designated at fair value through profit and loss .

(4) The decrease in tax expenses in 2018 is primarily attributed to the decrease in deferred tax expenses due to the decrease in the profit from adjustment of the fair value of investment properties in the present period compared with the corresponding period and a decrease in current tax expenses as a result of the decrease in the rate of companies tax. The increase in the Group's income tax expenses in Q4/2018, is mostly attributed to increase in deferred tax expenses due to the increase in profit resulting from fair value adjustments of investment property in the current period compared with the corresponding period.

## 6.5. Cash Flows

The following table shows the cash flows generated by the Group in Y2018 compared with Y2017:

| Annual Cash Flows | | |
|---|---|---|
| Year | 2018 | 2017 |
| Net cash flows generated by the Group from current operations (1) | 1,266 | 1,219 |
| Net cash flows used by the Group for investment activities (2) | (1,422) | (349) |
| Net cash flows used by the Group for financing activities (3) | (205) | (506) |

Figures are presented in millions of NIS.

(1) Most of the cash flow in the period and in the same period last year resulted from the operating profit of the income-producing real estate in the sum of approx. NIS 1,523 million (approx. NIS 1,385 million in the corresponding period), plus net senior housing deposits and excluding paid income taxes.

(2) Most of the cash flow in the Report Period was used for purchase of and investment in investment properties and investment properties under construction in the sum of approx. NIS 1,716 million, net of interest and dividend received, a decrease in short-term deposits and the revenues from the sale of Pi-Glilot. Most of the cash flow in the same period last year was used for the purchase of and investment in investment properties and investment properties under construction in the sum of approx. NIS 1,065 million, net of a decrease in short-term deposits and net proceeds from the disposition of Bank Leumi shares.

(3) Most of the cash flow in the Report Period was used for the distribution of dividend in the sum of approx. NIS 520 million. Most of the decrease relative to the same period last year derives from a decrease in the repayment of bonds, long-term loans and short-term credit (net) in the sum of approx. NIS 374 million.

The following table shows the cash flows generated by the Group in Q4/2018 compared with Q4/2017:

| Quarterly Cash Flows | | |
|---|---|---|
| Quarter | Q4/2018 | Q4/2017 |
| Net cash flows generated by the Group from current operations (1) | 254 | 273 |
| Net cash flows used by the Group for investment activities (2) | (159) | (228) |
| Net cash flows used by the Group from financing activities (3) | (83) | (87) |

Figures are presented in millions of NIS.

(1) The cash flow in the quarter and in the same quarter last year chiefly resulted from the operating profit of the income-producing real estate in the sum of approx. NIS 388 million (approx. NIS 360 million in the corresponding period), plus net senior housing deposits and excluding paid income taxes.

(2) Most of the cash flow in Q4/2018 was used for the purchase of and investment in investment properties and investment properties under construction in the sum of approx. NIS 209 million, net of received interest and dividend and proceeds from the sale of Pi-Glilot. Most of the cash flow in the same quarter last year was used for purchase of and investment in investment properties and investment properties under construction in the sum of approx. NIS 393 million, net of a decrease in short-term deposits.

(3) Most of the change relative to the same period last year derives from a decrease in the repayment of long-term loans and short-term credit (net), offset by paid interest.

# 7 | EXPOSURE TO AND MANAGEMENT OF MARKET RISKS

7 |

## 7.1. General

It is noted that the Company's financial statements present no separate reportable segment which is a "financial operating segment" and as of December 31, 2018 the Company has no "material financial operations" as stated in Regulation 10(b)(7) of the Regulation.

## 7.2. Description of Market Risks

For details with respect to the Company's market risks, see Notes 32 and 33 to the financial statements as of December 31, 2018.

## 7.3. The Company's Policy on Market Risk Management

For details with respect to the Company's market risk management, see Notes 32 and 33 to the financial statements as of December 31, 2018.

## 7.4. Policy Implementation and Oversight

At least once per quarter, the finance committee and the board of directors discuss the Company's exposure to market risks and the actions taken by the Company's management, and, to the extent necessary, set quantitative criteria and restrictions. The Company's management routinely examines the operation scopes and the risk deriving from the operations.

## 7.5. Analysis of Sensitivity Tests and Effects on the Fair Value of Hedging Transactions, Exchange Rates, Interest Rates and Financial Instruments

The Group conducts tests of sensitivity to changes in cap rates affecting the fair value of investment properties.

For details, see Annex A to this Chapter.

# 8 | CORPORATE GOVERNANCE ASPECTS

## 8 |

For details on aspects of the Company's corporate governance, including a corporate governance questionnaire, compensation of senior officers, contributions policy, details regarding the internal auditor, the auditor and an internal enforcement program at the Company, see the "Corporate Governance" chapter attached to Chapter E hereof. For details with respect to the Company's directors, see the "Additional Details" chapter attached as Chapter D hereof.

# 9 | PROVISIONS ON DISCLOSURE IN RELATION TO THE COMPANY'S FINANCIAL REPORTING

9 |

## 9.1. Report on the Group's Liabilities

A report on the Group's liabilities, in accordance with section 9D of the Regulations is attached in a separate report form concurrently with the release of this Report.

## 9.2. Litigation

For details with respect to litigation, see Note 31 to the financial statements.

## 9.3. Disclosure of Highly Material Valuations

A directive of the Israel Securities Authority (ISA)[21] determines that a material valuation is a valuation that fulfills one of the following criteria: (1) The subject-matter of the valuation represents at least 5% of the company's total assets as presented in the consolidated statement of financial position as of the last day of the report period (the "Balance Sheet Test") (2) The effect of the change in value that results from the valuation on the net profit or the comprehensive income, as applicable, represents at least 5% of the company's respective total net profit or comprehensive profit in the report period and also represents at least 2.5% of the company's equity as of the end the report period[22] (the "Consequence Test"). In addition, the directive specifies that a highly material valuation, which is required to be attached to the financial statements of the reporting corporation, is a valuation of double materiality (10%, rather than 5%; and 5%, rather than 2.5%).

The ISA has also determined that where the valuation satisfies the quantitative tests, but qualitative considerations led to a different decision by the corporation, and it is decided not to attach it, the corporation will disclose its decision, while specifying the results of the quantitative tests and the reasons and considerations that underpinned such decision.

As of the date of the Report, the Company's board of directors has adopted the parameters determined by the ISA, as specified above, with respect to the attachment of a highly material valuation.

As of the date of the Report, and following an examination of the above determination, it transpires that the Company has no valuation that is highly material which should be attached to the Report.

## 9.4. Subsequent Events

See Note 37 to the financial statements.

## 9.5. Financials attributable to the Company as a Parent Company

In accordance with Section 9C of the Regulations, financials out of the consolidated financial statements attributable to the Company as a parent company are attached with the auditor's opinion, in Chapter C.

[21] Legal statement no. 105-23 regarding parameters for testing of the materiality of valuations, last updated in July 2014, and clarification to legal statement no. 105-23 regarding parameters for testing of the materiality of valuations: Q&A's last upated in December 2018.

[22] Referring to the effect of the subject matter of the valuation after the tax effect, if any, and in absolute values.

## 9.6. Note on Forward-Looking Information

*The Company's intentions mentioned in the introduction to the board of directors' report and the highlights to the board of directors' report, inter alia, in relation to the use of business opportunities and expansion of the operations, liquidity, financing sources and net financing expenses, the pace of progress of projects under construction, the projected costs of their construction, the effects of the economic situation on the Company's operating segments and with respect to the possibility of converting short-term debt into long-term debt and/or obtaining financing, are forward-looking information as defined in the Securities Law, which is based on the Company's plans as of the date of the Report, the Company's estimations with respect to developments in the markets, inflation levels and projected cash flows and on the conditions and possibilities of obtaining credit on the date of the Report.*

*Such estimations may not materialize, in whole or in part, or materialize in a manner that materially differs from the Company's estimations. The principal factors that may affect the above are: changes in the capital market that will affect the conditions and possibilities of obtaining credit, changes in the Company's plans, including use of future available liquid balances for the purpose of seizing business opportunities, changes in the advantageousness of holding various investment channels or the advantageousness of use of various financing channels, delays in the obtainment of permits or approvals required for the progress of projects under construction, changes in the regulation related to the Company's business, including planning and building regulation, an increase in the prices of construction materials, changes in the CPI, deterioration of the Israeli or U.S. economy and decline into severe recession, and the Company or any of the Group's companies encountering financing or other difficulties, in a manner affecting the Company's cash flow.*

The Company’s board of directors and management wish to express their high regard for the Company’s officers, the managements of the various companies of the Group and their employees, for their welcome contribution to the Group’s achievements in 2018.

| | |
|---|---|
| Danna Azrieli, Chairman of the Board | Eyal Henkin, CEO |

Date: March 19, 2019

# Annex A

## Sensitivity Tests

## December 31, 2018

## Annex A – Sensitivity Tests

## Sensitivity to changes in the interest rates of the cap rates of investment property as of December 31, 2018

| | Loss from changes in market factor | | | Fair value of asset | Profit from changes in market factor | | | Value determination method |
|---|---|---|---|---|---|---|---|---|
| | NIS in millions | NIS in millions | NIS in millions | NIS in millions | NIS in millions | NIS in millions | NIS in millions | NIS in thousands |
| **Change Rate** | **Absolute 2% Increase** | **10% Increase** | **5% Increase** | | **5% Decrease** | **10% Decrease** | **Absolute 2% Decrease** | |
| **Weighted Cap Rate:** | | | | | | | | |
| 5.75% - 6.50% | (161) | (61) | (32) | 685 | 35 | 74 | 312 | DCF method |
| 6.75% - 7.25% | (3,680) | (1,498) | (784) | 16,278 | 867 | 1,829 | 6,633 | DCF method |
| 7.26% - 8% | (1,190) | (503) | (263) | 5,295 | 291 | 614 | 2,075 | DCF method |
| 8.01% - 8.5% | (84) | (39) | (21) | 392 | 23 | 48 | 137 | DCF method |
| 8.75% | (120) | (58) | (31) | 1,687 | 33 | 70 | 183 | DCF method |
| Investment property and investment property under construction | (5,235) | (2,159) | (1,131) | 24,337 | 1,249 | 2,635 | 9,340 | |

# Annex B

## Extended Standalone Financial Statements as of December 31, 2018

# Azrieli Group Ltd.

## Extended Standalone Financial Statements

### Annex B

The Company's extended standalone financial statements are the condensed Company's statements presented according to the IFRS rules, except for the investments in Granite and in Azrieli eCommerce which are presented based on the equity method *in lieu* of consolidation of their statements with the Company's statements (all other investments are presented with no change relative to the statement presented pursuant to the IFRS rules). These statements are not separate statements within the meaning thereof in IAS 27, nor separate financial statements pursuant to Regulation 9C of the Securities Regulations (Periodic and Immediate Reports), 5730-1970. The statements are not part of the information that is required to be published according to securities laws. However, the Company's management believes that analysts, investors, shareholders and bond holders may gain valuable information from the presentation of such figures.

The figures in this annex have not been audited or reviewed by the Company's auditors.

**Balance sheet**:

| | As of December 31 | |
|---|---|---|
| | 2018 | 2017 |
| | NIS in millions | NIS in millions |
| **Assets** | | |
| **Current Assets** | | |
| Cash and cash equivalents | 639 | 1,022 |
| Short-term deposits and investments | 7 | 105 |
| Trade accounts receivable | 83 | 59 |
| Other receivables | 133 | 195 |
| Current tax assets | 100 | 20 |
| | 962 | 1,401 |
| Held for sale assets | 450 | 40 |
| **Total Current Assets** | 1,412 | 1,441 |
| **Non-Current Assets** | | |
| Investment in investee companies | 734 | 792 |
| Loans and receivables | 334 | 283 |
| Financial assets | 1,227 | 1,685 |
| Investment property and investment property under construction | 27,452 | 25,206 |
| Fixed assets | 195 | 171 |
| Intangible assets | 84 | 85 |
| Deferred tax assets | 1 | 1 |
| **Total Non-Current Assets** | 30,027 | 28,223 |
| **Total Assets** | 31,439 | 29,664 |

# Azrieli Group Ltd.

## Extended Standalone Financial Statements

### Annex B

**Balance Sheet - Contd.**

| | As of December 31 | |
|---|---|---|
| | 2018 | 2017 |
| | NIS in millions | NIS in millions |
| **Liabilities and Capital** | | |
| **Current Liabilities** | | |
| Credit and current maturities from financial corporations and bonds | 1,492 | 1,443 |
| Trade payables | 253 | 218 |
| Payables and other current liabilities | 375 | 364 |
| Deposits from senior housing tenants | 839 | 689 |
| Current tax liabilities | 2 | 4 |
| **Total Current Liabilities** | 2,961 | 2,718 |
| **Non-Current Liabilities** | | |
| Loans from financial corporations | 2,191 | 2,268 |
| Bonds | 5,886 | 5,122 |
| Other liabilities | 63 | 52 |
| Deferred tax liabilities | 3,219 | 3,187 |
| **Total Non-Current Liabilities** | 11,359 | 10,629 |
| **Capital** | | |
| Ordinary share capital | 18 | 18 |
| Share premium | 2,518 | 2,518 |
| Capital reserves | 634 | 531 |
| Retained earnings | 13,907 | 13,214 |
| **Total equity attributable to the shareholders of the Company** | 17,077 | 16,281 |
| **Non-controlling interests** | 42 | 36 |
| **Total Capital** | 17,119 | 16,317 |
| **Total Liabilities and Capital** | 31,439 | 29,664 |

# Azrieli Group Ltd.

## Extended Standalone Financial Statements

### Annex B

**Income Statement:**

| | For the year ended December 31 | |
|---|---|---|
| | 2018 | 2017 |
| | NIS in millions | NIS in millions |
| **Revenues:** | | |
| From rent, management and maintenance fees | 2,069 | 1,875 |
| Net profit from adjustment of fair value of investment property and investment property under construction | 218 | 500 |
| Financing | 6 | 81 |
| Share in results of associates, net of tax | 20 | 21 |
| Other | 93 | 127 |
| **Total Revenues** | 2,406 | 2,604 |
| **Costs and Expenses** | | |
| Cost of revenues from rent, management and maintenance fees | 543 | 484 |
| Sales and Marketing | 49 | 44 |
| General and Administrative | 80 | 70 |
| Financing | 234 | 161 |
| Others | 4 | 4 |
| **Total Costs and Expenses** | 910 | 763 |
| **Income before income taxes** | 1,496 | 1,841 |
| Taxes on income | (275) | (393) |
| **Income from continuing operations per year, including the minority** | 1,221 | 1,448 |
| Loss from discontinued operations per year, including the minority | (2) | - |
| **Net Profit for the year, including the minority** | 1,219 | 1,448 |

# Annex C

## Designated Disclosure to Bondholders

# Annex C - Designated Disclosure to the Bondholders

## Set forth below are details regarding the bonds of the Company that are held by the public

| Series | Date of the Issue | Par Value on the Date of the Issue | Par Value on the Report Date | Par Value on the Report Date, including Linkage | Amount of Interest Accrued by the Report Date | Value in the Financial Statements | Market Cap | Type of Interest | Annual Interest Rate | Principal Payment Dates | Interest Payment Dates | Linkage Terms | Details regarding the Trustee |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | NIS in millions | | | | | | | | | | | | |
| Series B | February 10, 2015 | 623.3 | 1,056.7 | 1,059.8 | 1.7 | 1,046.8 | 1,061.7 | Fixed | 0.65 | April 1 in the years 2016 to 2025 (inclusive) | From October 1, 2015 and subsequently April 1st and October 1st in the years 2016 to 2025 (inclusive). | Linkage (principal and interest) to the rise in the CPI for December 2014* | Name of the trust company: Hermetic Trust (1975) Ltd.;<br><br>Address: Champion Tower, 13th floor, 30 Sheshet Hayamim Road, Bnei Brak.<br><br>Tel: -035274867;<br><br>Fax: 03-5271039;<br><br>E-mail address: hermetic@hermetic.co.il<br><br>Contact person at the trustee: Dan Avnon or Meirav Ofer. |
| | June 23, 2015 | 600.3 | | | | | | | | | | | |
| | March 30, 2017 | 228.8 | | | | | | | | | | | |
| Series C | Sept. 6, 2015 | 1,005.1 | 1,065.7 | 1,068.8 | 8.8 | 1,063.1 | 1,122.5 | Fixed | 1.64 | July 1 in the years 2018 to 2027 (inclusive) | From July 1, 2016, twice a year, on January 1st and July 1st in each of the years 2016 to 2027 (inclusive). | Linkage (principal and interest) to the rise in the CPI for July 2015* | |
| | March 30, 2017 | 179.0 | | | | | | | | | | | |
| Series D | July 7, 2016 | 2,194.1 | 4,362.9 | 4,432.9 | 29.1 | 4,410.8 | 4,405.1 | Fixed | 1.34 | From July 5, 2018 twice a year on January 5 and July 5 of each of the years 2018 through 2030 | From January 2017 twice a year on January 5 and July 5 of each of the years 2017 through 2030 | Linkage (principal and interest) to the rise in the CPI for May 2016* | |
| | March 30, 2017 | 983.6 | | | | | | | | | | | |
| | February 1, 2018 | 1,367.0 | | | | | | | | | | | |
| Total | | **7,181.2** | **6,485.3** | **6,561.5** | **39.6** | **6,520.7** | **6,589.3** | | | | | | |

* The Series B, Series C, Series D Bonds (the "**Company's Bond Series**") are protected, such that if the known index on the relevant payment due date is lower than the base index (stated in the table), the payment index will be the base index.

* This Annex C provides the details and data required in respect of the Company's Bond Series in circulation as of the date of the report. For details on the Company's Series E & F bonds, that were issued by the Company after the date of the report, see Note 19B(4) to Chapter C hereof.

Further details regarding the bonds of the Company held by the public:

1. The Company's Bond Series are material to the Company and are not secured by any collateral.

2. The Company will be entitled, at its sole discretion, to perform (partial or full) early redemption of the Company's Bond Series. For details, see Section 9.2 of the terms and conditions overleaf in the indentures of each of the Company's Bond Series, and as follows:

3. With respect to the Series B Bond indenture and the Series C Bond indenture, both of which were attached to the shelf offering report that was published by the Company, see the Company's report dated March 29, 2017 (Ref.: 2017-01-032703).

4. With respect to the Series D Bond indenture which was attached to the shelf offering report that was published by the Company, see the Company's report dated July 5, 2016 (ref.: 2016-01-075079).

5. The reports mentioned in Sections 3-4 above are included (the aforesaid sections) herein by way of reference.

6. At the end of and during the Reporting Period, the Company has fulfilled all of the terms and conditions and undertakings according to the indentures of the Company's Bond Series, and no conditions establishing grounds for acceleration of the Company's Bond Series have been fulfilled.

7. For details regarding an undertaking that the Company assumed in the framework of the Company's Bond Series, see Sections 5.2-5.6 of the indentures for the Company's Bond Series.

8. For further details regarding the terms and conditions of the Company's Bond Series, including an undertaking for meeting financial covenants and limitations with respect to the distribution of a dividend, see Note 19B to Chapter C hereof.

## Rating of the bonds of the Company held by the public:

| Series | Name of Rating Company | Rating Set on the Date of the Issue | Rating Set as of the Report Release Date | Date of Issuance of the Current Rating | Additional Ratings Set between the Date of the Issue and the Report Date | |
|---|---|---|---|---|---|---|
| | | | | | Rating | Date of Rating |
| **Series B** | Ma'alot | AA+ stable | AA+ stable | March 28, 2017(*) | AA+ stable<br>AA+ stable | June 21, 2015<br>March 27, 2017 |
| **Series C** | Ma'alot | AA+ stable | AA+ stable | March 28, 2017(*) | AA+ stable | September 3, 2015<br>March 27, 2017 |
| **Series D** | Midroog | Aa1/stable outlook | Aa1/stable outlook | January 31, 2018(**) | Aa1/stable outlook<br>Aa1/stable outlook<br>Aa1/stable outlook<br>Aa1/stable outlook<br>Aa1/stable outlook | July 20, 2016<br>March 27, 2017<br>March 28, 2017<br>December 31, 2017<br>January 28, 2018 |

* For Ma'alot's rating report on the Company's Series B and C Bonds, see the Company's immediate report of March 28, 2017 (Ref.: 2017-01-030966), which is included herein by way of reference.
** For Midroog's rating report on the Company's Series D Bonds, see the Company's immediate report of January 31, 2018 (Ref.: 2018-15-010804), which is included herein by way of reference.

AZRIELI GROUP

# Consolidated Financial Statements

## Dated 31 December 2018

# Part C

# Azrieli Group Ltd.

**Consolidated Financial Statements**
**For the Year 2018**

## C o n t e n t s

**Independent Auditors' Report to the Shareholders of**
# Azrieli Group Ltd.
**Regarding Audit of Components of Internal Control over Financial Reporting pursuant to Section 9B(c) of the Securities Regulations (Periodic and Immediate Reports), 5730-1970**

We have audited components of internal control over financial reporting of **Azrieli Group Ltd. and subsidiaries** (jointly, the "**Company**") as of December 31, 2018. These components of control were determined as explained in the following paragraph. The Company's Board of Directors ("**Board**") and Management are responsible for maintaining effective internal control over financial reporting and for their assessment of the effectiveness of the components of internal control over financial reporting, attached to the periodic report as of the above date. Our responsibility is to express an opinion on the components of internal control over financial reporting of the Company, based on our audit.

The components of the internal control over financial reporting that were audited were determined pursuant to Audit Standard 104 of the Institute of Certified Public Accountants in Israel "Audit of Components of Internal Control over Financial Reporting", including the amendments thereto ("**Audit Standard 104**"). These Components are: (1) Entity-level controls, including controls over the financial reporting and closing process and ITGCs; (2) Controls over investment property; (3) Controls over rent revenues from investment property; (4) Controls over revenues from gas customers of Supergas - Israeli Gas Distribution Company Ltd.; (all referred to hereafter jointly as the "**Audited Components of Control**").

We conducted our audit pursuant to Audit Standard 104. This Standard requires that we plan and perform the audit with the purpose of identifying the Audited Components of Control, and to obtain reasonable assurance about whether these components of control were effectively maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, identifying the Audited Components of Control, assessing the risk that a material weakness exists in the Audited Components of Control, and testing and evaluating the design and operating effectiveness of such components of control, based on the assessed risk. Our audit of such components of control also included performing such other procedures as we considered necessary in the circumstances. Our audit only referred to the Audited Components of Control, as opposed to internal control over all of the material processes in connection with the financial reporting, and therefore our opinion refers only to the Audited Components of Control. In addition, our audit did not address mutual effects between the Audited Components of Control and non-audited controls, and therefore, our opinion does not take into consideration such possible effects. We believe that our audit provides a reasonable basis for our opinion in the context described above.

Because of its inherent limitations, internal control over financial reporting in general and components thereof in particular, may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, based on our audit, the Company effectively maintained, in all material respects, the Audited Components of Control as of December 31, 2018.

We have also audited, based on Generally Accepted Auditing Standards in Israel, the Consolidated Financial Statements of the Company as of December 31, 2018 and 2017, and for each of the three years in the period ended December 31, 2018, and our report of March 19, 2019, included an unqualified opinion on those financial statements based on our audit and on the other auditors' reports.

**Brightman Almagor Zohar & Co.**
**Certified Public Accountants (Israel)**
**Member of Deloitte Touche Tohmatsu Limited**

**Tel Aviv, March 19, 2019**

**Independent Auditors' Report to the Shareholders of**
**<u>Azrieli Group Ltd.</u>**

We have audited the accompanying Consolidated Statements of Financial Position of **Azrieli Group Ltd.** (the "**Company**") as of December 31, 2018 and 2017 and the Consolidated Statements of Comprehensive Income, of Changes in Capital, and of Cash Flows for each of the years in the three-year period ended December 31, 2018. The Company's Board and Management are responsible for these Financial Statements. Our responsibility is to express an opinion on these Financial Statements based on our audit.

We did not audit the financial statements of consolidated companies, whose consolidated assets constitute approx. 3% of the total consolidated assets as of December 31, 2018 and 2017, and whose consolidated income from continuing operations constitute approx. 23%, approx. 22% and approx. 22% of the total consolidated income for the years ended December 31, 2018, 2017 and 2016, respectively. In addition, we did not audit the Group’s share in loss from discontinued operations of formerly consolidated companies which amounted to a sum of approx. NIS 2 million and NIS 9 million for the years ended December 31, 2018 and 2016, respectively. The financial statements of such companies were audited by other auditors whose reports were provided to us, and our opinion, insofar as it relates to amounts that have been included in respect of such companies, is based on the reports of the other auditors.

We conducted our audit in accordance with Generally Accepted Auditing Standards in Israel, including standards set in the Accountants Regulations (Mode of Operation of Accountants) 5733-1973. 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 Board and Management, as well as evaluating the overall financial statement presentation. We believe that our audit and the reports of other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audit and on the reports of other auditors, the Financial Statements referred to above present fairly, in all material respects, the financial position of the Company and of its subsidiaries as of December 31, 2018 and 2017 and the results of their operations, the changes in their equity and their cash flows for each of the years in the three-year period ended December 31, 2018 in accordance with International Financial Reporting Standards (IFRS) and the provisions of the Securities Regulations (Annual Financial Statements), 5770-2010.

We have also audited, pursuant to Audit Standard 104 of the Institute of Certified Public Accountants in Israel “Audit of Components of Internal Control over Financial Reporting”, components of the Company’s internal control over financial reporting as of December 31, 2018 and our report of March 19, 2019 included an unqualified opinion on the effective maintenance of such components.

**Brightman Almagor Zohar & Co.**
**Certified Public Accountants (Israel)**
**Member of Deloitte Touche Tohmatsu Limited**

**Tel Aviv, March 19, 2019**

# Azrieli Group Ltd.
## Consolidated Statements of Financial Position

| | Note | As of December 31 | |
|---|---|---|---|
| | | 82 0 1 | 72 0 1 |
| | | NIS in millions | NIS in millions |
| **ASSETS** | | | |
| **Current assets** | | | |
| Cash and cash equivalents | 4 | 716 | 1,064 |
| Short-term deposits and investments | 4 | 47 | 145 |
| Trade accounts receivable | 5 | 342 | 285 |
| Other receivables | 6 | 159 | 226 |
| Inventory | 7 | 66 | 64 |
| Current tax assets | 28 | 105 | 29 |
| | | 1,435 | 1,813 |
| Assets held for sale | 11B | 450 | 127 |
| **Total current assets** | | 1,885 | 1,940 |
| **Non-current assets** | | | |
| Investments and loans to associates | | 100 | 86 |
| Investments, loans and other receivables | 10 | 343 | 346 |
| Financial assets | 11 | 1,228 | 1,685 |
| Long-term receivables in respect of franchise arrangements | 12 | 46 | 50 |
| Investment property and investment property under construction | 13 | 27,452 | 25,206 |
| Fixed assets | 14 | 530 | 500 |
| Intangible assets | 15 | 296 | 310 |
| Deferred tax assets | 28 | 15 | 20 |
| **Total non-current assets** | | 30,010 | 28,203 |
| **Total assets** | | 31,895 | 30,143 |

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

## Azrieli Group Ltd.
### Consolidated Statements of Financial Position
**(Continued)**

| | Note | As of December 31<br>82 0 1<br>NIS in millions | <br>72 0 1<br>NIS in millions |
|---|---|---|---|
| **LIABILITIES AND CAPITAL** | | | |
| **Current liabilities** | | | |
| Credit and current maturities from financial corporations and bonds | 19 | 1,565 | 1,511 |
| Trade payables | 16 | 342 | 296 |
| Other payables | 17 | 225 | 201 |
| Deposits from customers | 18 | 942 | 792 |
| Provisions | | 12 | 13 |
| Current tax liabilities | 28 | 6 | 16 |
| **Total current liabilities** | | 3,092 | 2,829 |
| **Non-current liabilities** | | | |
| Loans from financial corporations | 19 | 2,226 | 2,304 |
| Bonds | 19 | 6,165 | 5,435 |
| Other liabilities | 20 | 67 | 55 |
| Deferred tax liabilities | 28 | 3,224 | 3,199 |
| **Total Non-Current Liabilities** | | 11,682 | 10,993 |
| **Capital** | 21 | | |
| Ordinary share capital | | 18 | 18 |
| Share premium | | 2,518 | 2,518 |
| Capital reserves | | 634 | 531 |
| Retained earnings | | 13,907 | 13,214 |
| **Total equity attributable to the shareholders of the company** | | 17,077 | 16,281 |
| **Non-controlling interests** | | 44 | 40 |
| **Total Capital** | | 17,121 | 16,321 |
| **Total Liabilities and Capital** | | 31,895 | 30,143 |

| March 19, 2019 | | | |
|---|---|---|---|
| **Date of approval of the Financial Statements** | **Danna Azrieli<br>Chairman of the Board** | **Eyal Henkin<br>CEO** | **Irit Sekler-Pilosof<br>CFO** |

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

# Azrieli Group Ltd.
## Consolidated Statements of Income or Other Comprehensive Loss and Profit

| | Note | 2018 | 2017 | 2016 |
|---|---|---|---|---|
| | | As of the year ended December 31 | | |
| | | NIS in millions | NIS in millions | NIS in millions |
| **Revenues** | | | | |
| From rent, management and maintenance fees | | 2,063 | 1,868 | 1,745 |
| From sales, labor and services | 22 | 758 | 724 | 660 |
| Net profit from adjustment to fair value of investment property and investment property under construction | 13 | 218 | 500 | 711 |
| Financing | 27 | 17 | 94 | 49 |
| Other | 26 | 95 | 129 | 14 |
| **Total revenues** | | 3,151 | 3,315 | 3,179 |
| **Costs and Expenses** | | | | |
| Costs of revenues from rent, management and maintenance fees | 23 | 543 | 484 | 445 |
| Costs of revenues from sales, labor and services | 23 | 500 | 474 | 420 |
| Sales and marketing | 24 | 200 | 192 | 172 |
| General and administrative | 25 | 123 | 114 | 104 |
| Share in results of associates, net of tax | | 6 | 6 | 8 |
| Financing | 27 | 258 | 184 | 159 |
| Other | | 7 | 5 | 5 |
| **Total costs and expenses** | | 1,637 | 1,459 | 1,313 |
| **Income before income taxes** | | 1,514 | 1,856 | 1,866 |
| Taxes on income | 28 | (293) | (408) | (49) |
| **Income from continued operations** | | 1,221 | 1,448 | 1,817 |
| Loss from discontinued operations, net of tax | 8 | (2) | - | (9) |
| **Net profit for the year** | | 1,219 | 1,448 | 1,808 |
| **Other comprehensive income:** | | | | |
| **Amounts that will not be carried in the future to the income statement, net of tax:** | | | | |
| Change in fair value of financial assets, net of tax | | 11 | 204 | 116 |
| **Amounts that were carried or will be carried in the future to the income statement, net of tax:** | | | | |
| Amounts that were carried to the income statement from disposition of financial assets, net of tax | | - | (62) | (20) |
| Translation differences from foreign operations | | 95 | (114) | (11) |
| **Total** | | 95 | (176) | (31) |
| **Other comprehensive income for the year, net of tax** | | 106 | 28 | 85 |
| **Total comprehensive income for the year** | | 1,325 | 1,476 | 1,893 |

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

# Azrieli Group Ltd.

## Consolidated Statements of Income or Other Comprehensive Loss and Profit

**(Continued)**

| | As of the year ended December 31 | | |
|---|---|---|---|
| | **2018** | **2017** | **2016** |
| | **NIS in millions** | **NIS in millions** | **NIS in millions** |
| **Net profit for the year attributable to:** | | | |
| Shareholders of the company | 1,218 | 1,456 | 1,810 |
| Non-controlling interests | 1 | (8) | (2) |
| | 1,219 | 1,448 | 1,808 |
| **Total comprehensive income for the year attributable to:** | | | |
| Shareholders of the company | 1,321 | 1,488 | 1,895 |
| Non-controlling interests | 4 | (12) | (2) |
| | 1,325 | 1,476 | 1,893 |
| | **NIS** | **NIS** | **NIS** |
| **Basic and diluted earnings (in NIS) per one ordinary share of par value NIS 0.1 each attributable to shareholders of the company:** | | | |
| Continued operations | 10.06 | 12.01 | 15.00 |
| Discontinued operations | (0.02) | - | (0.07) |
| | 10.04 | 12.01 | 14.93 |
| Average weighted share capital used in calculating the basic and diluted earnings per share | 121,272,760 | 121,272,760 | 121,272,760 |

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

# Azrieli Group Ltd.
## Consolidated Statements of Changes in Capital

| | For the year ended December 31, 2018 | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Share Capital | Share premium | Capital reserve for changes in fair value of investments in equity instruments designated at fair value through other comprehensive income | Capital reserve for translation differences from foreign operations | Other capital reserves | Retained earnings | Total attributable to share-holders of the company | Non-controlling interests | Total |
| | NIS in millions | | | | | | | | |
| **Balance as of January 1, 2018** | 18 | 2,518 | 629 | (91) | (7) | 13,214 | 16,281 | 40 | 16,321 |
| Effect of first application of IFRS 9 | - | - | - | - | - | (5) | (5) | - | (5) |
| Balance as of January 1, 2018, after retroactive adjustments and restatement | 18 | 2,518 | 629 | (91) | (7) | 13,209 | 16,276 | 40 | 16,316 |
| Net profit for year | - | - | - | - | - | 1,218 | 1,218 | 1 | 1,219 |
| Change in fair value of financial assets, net of tax | - | - | 11 | - | - | - | 11 | - | 11 |
| Translation differences from foreign operations | - | - | - | 92 | - | - | 92 | 3 | 95 |
| **Total comprehensive income for the year** | - | - | 11 | 92 | - | 1,218 | 1,321 | 4 | 1,325 |
| Dividend to the shareholders of the Company | - | - | - | - | - | (520) | (520) | - | (520) |
| **Total transactions with shareholders of the Company** | - | - | - | - | - | (520) | (520) | - | (520) |
| **Balance as of December 31, 2018** | 18 | 2,518 | 640 | 1 | (7) | 13,907 | 17,077 | 44 | 17,121 |

**The notes to the Financial Statements form an integral part thereof.**

## Azrieli Group Ltd.
### Consolidated Statements of Changes in Capital
### (Continued)

| | For the year ended December 31, 2017 | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Share Capital | Share premium | Revaluation fund for financial assets | Capital reserve for translation differences from foreign operations | Other capital reserves | Retained earnings | Total attributable to share-holders of the company | Non-controlling interests | Total |
| | NIS in millions | | | | | | | | |
| **Balance as of January 1, 2017** | 18 | 2,518 | 487 | 19 | (7) | 12,238 | 15,273 | 43 | 15,316 |
| Net profit for year | - | - | - | - | - | 1,456 | 1,456 | (8) | 1,448 |
| Change in fair value of financial assets, net of tax | - | - | 204 | - | - | - | 204 | - | 204 |
| Amounts that were carried to the income statement from disposition of financial assets, net of tax | - | - | (62) | - | - | - | (62) | - | (62) |
| Translation differences from foreign operations | - | - | - | (110) | - | - | (110) | (4) | (114) |
| **Total comprehensive income for the year** | - | - | 142 | (110) | - | 1,456 | 1,488 | (12) | 1,476 |
| Dividend to the shareholders of the Company | - | - | - | - | - | (480) | (480) | - | (480) |
| Investment of non-controlling interests in a subsidiary | - | - | - | - | - | - | - | 9 | 9 |
| **Total transactions with shareholders of the Company** | - | - | - | - | - | (480) | (480) | 9 | (471) |
| **Balance as of December 31, 2017** | 18 | 2,518 | 629 | (91) | (7) | 13,214 | 16,281 | 40 | 16,321 |

**The notes to the Financial Statements form an integral part thereof.**

# Azrieli Group Ltd.
## Consolidated Statements of Changes in Capital
**(Continued)**

| | For the year ended December 31, 2016 | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Share Capital | Share premium | Revaluation fund for financial assets | Capital reserve for translation differences from foreign operations | Other capital reserves | Retained earnings | Total attributable to share-holders of the company | Non-controlling interests | Total |
| | NIS in millions | | | | | | | | |
| **Balance as of January 1, 2016** | 18 | 2,518 | 391 | 30 | (14) | 10,828 | 13,771 | 99 | 13,870 |
| Net profit for year | - | - | - | - | - | 1,810 | 1,810 | (2) | 1,808 |
| Change in fair value of financial assets, net of tax | - | - | 116 | - | - | - | 116 | - | 116 |
| Amounts that were carried to the income statement from disposition of financial assets, net of tax | - | - | (20) | - | - | - | (20) | - | (20) |
| Translation differences from foreign operations | - | - | - | (11) | - | - | (11) | - | (11) |
| **Total comprehensive income for the year** | - | - | 96 | (11) | - | 1,810 | 1,895 | (2) | 1,893 |
| Dividend to the shareholders of the Company | - | - | - | - | - | (400) | (400) | - | (400) |
| Investment of non-controlling interests in a subsidiary | - | - | - | - | - | - | - | 4 | 4 |
| Acquisition of non-controlling interest in a subsidiary | - | - | - | - | 7 | - | 7 | (58) | (51) |
| **Total transactions with shareholders of the Company** | - | - | - | - | - | (400) | (393) | (54) | (447) |
| **Balance as of December 31, 2016** | 18 | 2,518 | 487 | 19 | (7) | 12,238 | 15,273 | 43 | 15,316 |

**The notes to the Financial Statements form an integral part thereof.**

# Azrieli Group Ltd.
## Consolidated Statements of Cash Flows

| | As of the year ended December 31 | | |
|---|---|---|---|
| | 2018 | 2017 | 2016 |
| | NIS in millions | NIS in millions | NIS in millions |
| **Cash Flows – Operating activities** | | | |
| Net profit for the year | 1,219 | 1,448 | 1,808 |
| Depreciation and amortization | 68 | 64 | 88 |
| Impairment of intangible assets | - | - | 32 |
| Forfeiture of senior housing residents' deposits | (22) | (21) | (17) |
| Net profit from adjustment to fair value of investment property and investment property under construction | (218) | (500) | (711) |
| Financing and other expenses (income), net | 142 | (46) | 116 |
| Profit from the sale of fixed assets, investment property and intangible assets, net | - | - | (1) |
| Share in losses of associates accounted for by the equity method | 6 | 6 | 8 |
| Tax expenses recognized in the income statement | 293 | 408 | 58 |
| Loss from disposition of investment in a subsidiary (Annex A) | - | - | 6 |
| Income taxes paid, net | (330) | (186) | (242) |
| Revaluation of financial assets designated at fair value through profit and loss | 8 | 4 | (4) |
| Change in inventory | (11) | (3) | (2) |
| Change in trade and other receivables | (49) | (48) | (4) |
| Change in receivables in respect of franchise arrangement | 4 | 2 | (11) |
| Change in trade and other payables | 12 | 24 | 93 |
| Receipt of deposits from senior housing residents | 184 | 112 | 101 |
| Return of deposits from senior housing residents | (42) | (45) | (28) |
| Change in provisions and employee benefits | 2 | - | - |
| **Net cash – operating activities** | 1,266 | 1,219 | 1,290 |

**The notes to the Financial Statements form an integral part thereof.**

## Azrieli Group Ltd.
### Consolidated Statements of Cash Flows
**(Continued)**

| | As of the year ended December 31 | | |
|---|---|---|---|
| | **2018** | **2017** | **2016** |
| | **NIS in millions** | **NIS in millions** | **NIS in millions** |
| **Cash Flows - Investment Activities** | | | |
| Proceeds from the disposition of fixed assets and intangible assets | 1 | 2 | 3 |
| Proceeds from the disposition of investment property | 36 | - | 5 |
| Advance payments on account of disposition of investment property | - | 8 | - |
| Purchase and investment in investment property and investment property under construction | (1,729) | (1,052) | (2,008) |
| Purchase of fixed assets and intangible assets | (81) | (86) | (118) |
| Investment in and provision of loans to associates | (17) | (15) | (17) |
| Change in short-term deposits | 97 | 514 | (618) |
| Change in restricted investments | - | 3 | - |
| Receipt of insurance indemnification | 50 | - | - |
| Income for the disposition of derivative financial instruments, net | - | - | 1 |
| Investment in financial assets designated at fair value through profit and loss, net | - | 3 | 5 |
| Provision of long-term loans | - | (1) | (3) |
| Collection of long-term loans | 23 | 6 | 16 |
| Interest and dividend received | 100 | 38 | 28 |
| Proceeds from disposition of financial assets, net | 87 | 233 | 80 |
| Acquisition of companies consolidated for the first time (Annex B) | - | 6 | (61) |
| Proceeds from disposition of investments in investee companies, net (Annex A) | - | 22 | 116 |
| Taxes paid for financial assets | (2) | (17) | - |
| Institutions in respect of the purchase of real estate | 13 | (13) | (7) |
| **Net cash - investment activities** | (1,422) | (349) | (2,578) |

**The notes to the Financial Statements form an integral part thereof.**

# Azrieli Group Ltd.
## Consolidated Statements of Cash Flows
**(Continued)**

| | As of the year ended December 31 | | |
|---|---|---|---|
| | **2018** | **2017** | **2016** |
| | **NIS in millions** | **NIS in millions** | **NIS in millions** |
| **Cash Flows - Financing Activities** | | | |
| Acquisition of non-controlling interests | - | - | (51) |
| Distribution of dividend to shareholders | (520) | (480) | (400) |
| Repayment of bonds | (492) | (645) | (410) |
| Issuance of bonds net of issue expenses | 1,399 | 1,354 | 2,177 |
| Receipt of long-term loans from financial corporations | 215 | 244 | 1,140 |
| Repayment of long-term loans from financial corporations | (456) | (742) | (885) |
| Short-term credit from banks and others, net | (147) | (66) | (309) |
| Repayment of deposits from customers | (7) | (7) | (4) |
| Deposits from customers that were received | 9 | 10 | 6 |
| Investment of non-controlling interests in a subsidiary | - | 5 | 4 |
| Interest paid | (206) | (179) | (199) |
| **Net cash - financing activities** | (205) | (506) | 1,069 |
| **Increase (decrease) in cash and cash equivalents** | (361) | 364 | (219) |
| **Cash and cash equivalents at the beginning of the year** | 1,064 | 715 | 935 |
| Change in net cash classified to disposal group held for sale | - | - | 1 |
| Effect of the changes in exchange rates on balances of cash held in foreign currency | 13 | (15) | (2) |
| **Cash and cash equivalents at the end of the year** | 716 | 1,064 | 715 |

(*) Non-cash transactions include a change in other payables in respect of acquisitions on credit of non-current assets in 2018 in the sum of NIS 34 million (in 2017 – NIS 39 million). In 2016, the non-cash transactions included a change in receivables due to the sale of an investment in an investee in the sum of NIS 125 million.

(**) With respect to cash flows from discontinued operations, see Note 8.

# Azrieli Group Ltd.
## Consolidated Statements of Cash Flows
**(Continued)**

| | As of the year ended December 31 | | |
|---|---|---|---|
| | 2018 | 2017 | 2016 |
| | NIS in millions | NIS in millions | NIS in millions |
| **Annex A -** | | | |
| **Proceeds from sale of investment in previously-consolidated Sonol Israel Ltd. (see Note 8):** | | | |
| Working capital (excluding cash and cash equivalents) | - | - | (181) |
| Investments and loans | - | - | 73 |
| Fixed and intangible assets, net | - | - | 684 |
| Prepaid long-term lease payments | - | - | 37 |
| Investment property | - | - | 12 |
| Deferred tax assets | - | - | 7 |
| Employee benefits and provisions | - | - | (72) |
| Long-term liabilities including current maturities | - | - | (312) |
| Loan provided (repaid) due to sale of the investment | - | 22 | (98) |
| Receivables due to sale of the investment | - | - | (28) |
| Loss from liquidation of investment in subsidiary | - | - | (6) |
| | - | 22 | 116 |
| **Annex B -** | | | |
| **Increase of our share in the partnerships in the U.S. (see Note13D(2)):** | | | |
| Working capital (excluding cash and cash equivalents) | - | (1) | - |
| Investment property | - | (124) | - |
| Fixed and intangible assets, net | - | (3) | - |
| Long-term liabilities including current maturities | - | 134 | - |
| | - | 6 | - |
| **Purchase of a company consolidated for the first time – Ahuzat Bayit Ra'anana – Retirement Home Ltd.:** | | | |
| Working capital (excluding cash and cash equivalents and short-term deposits) | - | - | (31) |
| Liabilities in respect of deposits from customers | - | - | 328 |
| Fixed and intangible assets, net | - | - | (13) |
| Investment property | - | - | (531) |
| Long-term liabilities including current maturities | - | - | 212 |
| | - | - | (35) |
| **Purchase of a company consolidated for the first time – Azrieli E-Commerce Ltd. (formerly Netex New Media Ltd.):** | | | |
| Working capital (excluding cash and cash equivalents) | - | - | 5 |
| Fixed and intangible assets, net | - | - | (80) |
| Long-term liabilities including current maturities | - | - | 38 |
| Payables due to purchase of an investment | - | | 11 |
| | - | - | (26) |
| **Purchase of a company consolidated for the first time – Bio Clean Air Innovation Ltd.:** | | | |
| Working capital (excluding cash and cash equivalents) | - | - | 6 |
| Fixed and intangible assets, net | - | - | (7) |
| Reserve for deferred taxes, net | - | - | 1 |
| | - | - | - |
| **Total purchase of companies consolidated for the first time** | - | 6 | (61) |

**The notes to the Financial Statements form an integral part thereof.**

## Note 1 - General

### A. General description of the Company and its operations:

Azrieli Group Ltd. (the "**Company**") is a company domiciled and incorporated in Israel and whose registered address is 1 Azrieli Center, Tel Aviv. The Company is traded on the TASE and is included in the Tel Aviv 35 Index and in the Tel Aviv Real Estate 15 Index. The Company has bonds that were issued to the public (Series B, Series C, Series D as well as Series E and F that were issued after the date of the Statement of Financial Position). The Group's Consolidated Financial Statements as of December 31, 2018 include those of the Company and of its subsidiaries (jointly, the "**Group**"), as well as the Group's rights in associates and in jointly-controlled entities.

As of the Report Release Date, Azrieli Holdings Inc., the controlling shareholder of the Company ("**Azrieli Holdings**"), directly and/or indirectly holds (through its holding of the entire share capital of Nadav Investments Inc. ("**Nadav Investments**")) (both private companies registered in Canada), approx. 55.62% of the Company's share capital and approx. 61.31% of the Company's voting rights.

As the Company was informed, on April 13, 2015, shares of Mr. David Azrieli OBM in Azrieli Holdings and in a Canadian holding corporation controlled by him ("**David Holding Corporation**") were distributed from his estate. Following such distribution, each one of Sharon Azrieli, Naomi Azrieli and Danna Azrieli, holds, directly and through David Holding Corporation, approx. 27.24% of the capital rights in Azrieli Holdings and approx. 33.13% of the voting rights in Azrieli Holdings, and they jointly hold approx. 81.73% of the capital rights in Azrieli Holdings and approx. 99.39% of the voting rights therein. The remainder of Azrieli Holdings' shares are mainly held by the Azrieli Foundation of Canada (an interested party of the Company), which following the distribution of the estate holds (indirectly, through a holding of shares of David Holding Corporation) approx. 15.93% of Azrieli Holdings' shares, with no voting rights (which constitutes, indirectly, a holding of approx. 8.86% of the capital rights of the Company), in addition to and separately from its direct holding of approx. 8.55% of the capital and voting rights in the Company.

As the Company was informed, on March 20, 2017, a shareholders' agreement (the "**2017 Agreement**") was signed between Sharon Azrieli, Naomi Azrieli and Danna Azrieli (in person and through companies controlled by them), the indirect controlling shareholders of the Company and directors thereof (the "**Controlling Shareholders**"). Additional parties to the 2017 Agreement are Azrieli Holdings, Nadav Investments and David Holding Corporation (the three "**Holding Corporations**"). The 2017 Agreement replaces and substitutes the former shareholders agreement made by the parties in November 2012 (the "**2012 Agreement**"), and it regulates the relations between the Controlling Shareholders, in person, and through the Holding Corporations, in respect of their rights in the Company. Similarly to the 2012 Agreement, the terms of the 2017 Agreement include agreements regarding the sale and transfer of shares in the Company and in the Holding Corporations, including a lock-up period, right of first refusal, right of first offer, co-sale right and an exclusion in connection with certain sales of shares (drip) on TASE. The 2017 Agreement further prescribes that the manner of use of the voting rights in the Company will be determined by the Controlling Shareholders (by a majority vote), provided however, that in respect of resolutions to appoint directors of the Company, each one of the Controlling Shareholders shall have the right to use the voting rights to appoint one director who will be determined by her, whereas the manner of use of the voting rights in the Company regarding resolutions to appoint additional directors, will be adopted by a majority vote. It is clarified, that the 2017 Agreement does not change the identity of the Company's controlling shareholders (including of Azrieli Holdings) nor their percentage holdings in the capital and in the voting rights in the Company, and that as of the Report Date, Sharon Azrieli, Naomi Azrieli and Danna Azrieli are the Company's controlling shareholders

## Note 1 – General (Cont.)

### A. General description of the Company and its operations: (Cont.)

The Company engages (both directly and through investee companies in which it invests and which it develops) primarily in the following operating segments:

**(1)** In development, acquisition, management and lease in the retail centers and malls in Israel segment.
**(2)** In development, acquisition, management and lease in the leasable office and other space in Israel segment.
**(3)** In acquisition, management and lease in income-producing property in the U.S. segment.
**(4)** In development, acquisition and operation of senior housing.
**(5)** In activities of alternative energy sources, water and wastewater through its holding in Granite Hacarmel Investments Ltd.

For details regarding additional business activities of the Company, see Note 36A.

### B. Definitions:

| | | |
|---|---|---|
| **Interested Parties** | - | As defined in the Securities Law, 5728-1968, and regulations thereunder. |
| **Controlling Shareholder** | - | As defined in the Securities Regulations (Annual Financial Statements), 5770-2010. |
| **Canit Hashalom** | - | Canit Hashalom Investments Ltd. |
| **Granite** | - | Granite Hacarmel Investments Ltd. |
| **GES** | - | GES Global Environmental Solutions Ltd. |
| **Supergas** | - | Supergas - Israeli Gas Distribution Company Ltd. |

## Note 2 - Significant accounting policies

### A. Declaration in respect of the application of the International Financial Reporting Standards (IFRS):

The Group's Consolidated Financial Statements have been prepared in accordance with the International Financial Reporting Standards (the "**IFRS Standards**") and the interpretations thereto, which have been published by the International Accounting Standards Board (IASB). The significant accounting policies that are detailed further on in this report have been applied in a consistent manner for all of the reporting periods that are presented in these Consolidated Financial Statements, except for changes in the accounting policies, which derived from the application of standards, amendments to standards and interpretation, which took effect or early adopted as of the date of the Financial Statements, as detailed in Note 2CC.

The consolidated Financial Statements were approved for publication by the Company’s Board on March 19, 2019.

**B.** The Financial Statements include the disclosure requirements in accordance with the Securities Regulations (Annual Financial Statements), 5770-2010 (the "**Financial Statements Regulations**").

### C. The operating cycle period:

The Group's operating cycle does not exceed 12 months.

### D. The format for the analysis of the expenses that have been recognized in the Statement of Comprehensive Income:

The Company's expenses in the Statement of Comprehensive Income are presented in accordance with a method of classification based on the nature of the activity to which the expense relates.

**Note 2 - Significant accounting policies (Cont.)**

**E. Foreign currency:**

**(1) The functional currency and the presentation currency**

The financial statements of each of the companies in the Group have been prepared in the currency of the main economic environment in which they operate, mainly NIS (the "**Functional Currency**"). For the purposes of the consolidation of the Financial Statements, the results and the financial position of each of the companies in the Group are presented in New Israeli Shekels (NIS), which is the Company's functional currency. The Company's Consolidated Financial Statements are presented in NIS in millions. On exchange rates and the changes therein in the course of the periods that are presented, see Note 2BB.

**(2) The translation of transactions other than in the functional currency**

In the preparation of the financial statements of each of the companies in the Group, transactions that were executed in currencies that are different from the Company's functional currency ("**Foreign Currency**") have been recorded in accordance with the exchange rates that were in force at the time of the transactions. At the end of each reporting period, monetary items that are stated in foreign currency are translated in accordance with the exchange rates in force as of that time. Non-monetary items that are measured at fair value and stated in foreign currency are translated in accordance with the exchange rate at the time at which the fair value was determined; non-monetary items that are measured in historical cost terms are translated in accordance with the exchange rates that were in force at the time of the execution of the transaction in respect of the non-monetary item.

**(3) The manner in which exchange differences are recorded**

Exchange differences are recognized in the income statement in the period in which they arise, except for the following cases:

- Exchange differences in respect of transactions that were designated for the hedging of certain foreign currency risks.

- Exchange differences in respect of financial items receivable or payable from foreign operations, whose settlement is not planned or expected to occur and accordingly they constitute part of the net investment in foreign operations, are recognized in the statement of other comprehensive income under the 'exchange differences in respect of foreign operations' item, and are carried to profit and loss at the time of the disposition of the net investment in foreign operations and upon partial disposition of the net investment in foreign business entailing loss of control.

**(4) The translation of the financial statements of foreign operations whose functional currency is different from the Shekel (the Group's functional currency) and is mainly U.S. dollars**

For the purposes of the presentation of the Consolidated Financial statements, the assets and the liabilities of foreign operations are presented in accordance with the exchange rate in force at the end of the reporting period. Income and expense items are translated in accordance with the average exchange rate for the reporting period unless there shall have been significant fluctuations in the exchange rates in the course of the period. In such a case, the translation of these items is done using the exchange rates at the time of the execution of the transactions, the exchange differences are recognized in the statement of comprehensive income under "translation differences from foreign operations". These translation differences are carried to the income statement on the disposition of the foreign business in respect of which they were created and upon partial disposition of foreign business entailing loss of control.

**Note 2 - Significant accounting policies (Cont.)**

**F. Consolidated Financial Statements:**

The Group's Consolidated Financial Statements include the financial statements of the Company and of entities that are directly or indirectly controlled by the Company. An investing company is controlling an investee company when it is exposed or has rights to variable yields deriving from its holding in the investee company and when it has the ability to have an effect on such yields through exercise of power on the investee company. This principle applies to all investee companies.

Financial statements of the consolidated companies that were prepared other than in accordance with the Group's accounting policies were adjusted, prior to their consolidation, to the accounting policies that have been implemented by the Group.

For the purposes of the consolidation, all inter-company transactions, balances, income and expenses have been eliminated in full.

**G. Non-controlling interests:**

Non-controlling interests are the capital in a subsidiary which cannot be attributed, either directly or indirectly, to the parent company.

Transactions with non-controlling interests, while retaining control – Transactions with non-controlling interests while retaining control are treated as equity transactions. Any difference between the consideration paid or received and the change in the non-controlling interests is carried to the share of the holders of the Company directly to a capital reserve from transactions with non-controlling interests in a consolidated company.

**H. Business combinations:**

The acquisition of activities and consolidated companies which constitute a business are presented while using the acquisition method. The cost of the business combination is presented as the aggregate fair value (as of the exchange date) of granted assets, incurred liabilities.

Transaction costs, which are directly related to the business combination are carried to the profit or loss when incurred.

The identified assets and liabilities of the purchased business, which meet the conditions for recognition under the (amended) IFRS 3 "Business Combinations", are recognized according to their fair value on the purchase date, other than a number of types of assets which are presented according to the provisions of the relevant standards.

Goodwill resulting from business combination is presented at the sum of the excess of the cost of the purchase over the Company's share in the net fair value of the identified assets, liabilities and contingent liabilities of the consolidated company that were recognized on the purchase date. If, after revaluation, the Group's rights in the net fair value of the identified assets, liabilities and contingent liabilities that were recognized, in total, exceed the cost of the business combination, the excess is immediately recognized in the profit or loss.

Non-controlling interest in the acquired entity are presented for the first time on the date of the business combination at the rate of their share in the fair value of the assets, liabilities and contingent liabilities of the acquired entity, excluding their share in goodwill.

**Note 2 - Significant accounting policies (Cont.)**

**I. Joint arrangements**:

"Joint arrangement" is a contractual agreement whereby the Group and other parties perform financial activity that is subject to joint control. Joint control is in place where the contractual arrangement includes a requirement whereby decisions pertaining to the transaction's financial and operational strategy, must be adopted unanimously by the parties which jointly control the joint transaction.

**Joint operation:**

A joint operation is a joint arrangement wherein the parties thereto have interests in the assets, and commitments with regards to the liabilities that are attributed to the arrangement.

In joint arrangements that constitute joint operations, the Group recognizes in the Group’s Statement of Financial Position its pro-rata share in the joint operation’s assets and liabilities, including assets that are held and liabilities that were formed jointly. The income statement includes the Group’s pro-rata share in the income and expenses of the joint operation, including income derived and expenses incurred jointly.

**J. Goodwill:**

Goodwill that derives from the acquisition of a consolidated company is presented in the framework of intangible assets and is measured at the level of the surplus of the cost of the acquisition over the Company’s share in the net fair value of the identified assets, liabilities and contingent liabilities of the consolidated company, which were recognized at the time of the acquisition.

Goodwill is initially recognized as an asset at cost and is measured in following periods as cost net of accumulated losses from impairment.

For the purposes of the testing for impairment, goodwill is allocated to each of the Group's cash generating units, which derive benefits from the synergies from the business combination. Cash generating units to which Goodwill has been allocated are tested for impairment each year or more frequently, where signs exist, which evidence a possible impairment of the unit, as aforesaid. Where the recoverable amount of a cash generating unit is lower than the carrying value of that unit, the loss from impairment is allocated firstly to the writing down of the carrying value of any goodwill whatsoever in respect of the cash generating unit. Thereafter, the balance of the impairment loss, if any remains, is allocated to the other assets making up the cash generating unit, in proportion to their book value. A loss from impairment of goodwill is not cancelled in following periods.

Upon a disposition of a consolidated company, the amount of the goodwill that is attributed to it is included in the determination of the profit or loss on the disposition.

**K. Non-current assets held for sale:**

Non-current assets which are classified as held for sale, with the exception of investment property which is presented by fair value, are measured by the lower of their book value and their fair value net of disposal costs.

In subsequent periods, depreciable assets that are classified as held for sale, are not depreciated periodically.

**Note 2 - Significant accounting policies (Cont.)**

**L. Discontinued Operations**

Operations that were realized or are classified as held for sale, constitute discontinued operations when representing a business operating segment or an operations' geographic region which is significant and separate, or when they constitute part of a single and adjusted planning for the disposal of a business operating segment or of an operations' geographic region which is significant and separate. Revenues and expenses which belong to discontinued operations are presented in the Statements of Profit or Loss and Other Comprehensive Income, Net, net of taxes on income during all of the periods presented as part of the "Income from discontinued operations (net of tax)" item. The cash flows from discontinued operations are jointly presented in the Discontinued Operations Note in all of the report periods presented, according to the classification of operating activities, investment activity and financing activity.

The comparative figures in Statements of Profit or Loss and Other Comprehensive Income from the results of the discontinued operations, are retroactively adjusted.

**M. Loss of Control**

Upon loss of control, the Group writes-off the assets and liabilities of the subsidiary, any non-controlling interest and other capital components attributable to the subsidiary. The difference between the consideration and the fair value of the investment balance and between the balances written-off, is recognized in profit and loss under the “Other income” item. The amounts recognized in equity through other comprehensive income in reference to such subsidiary are reclassified as profit or loss or as retained earnings, as would have been required had the subsidiary disposed of the relevant assets or liabilities itself.

**N. Financial instruments:**

**(1) Financial assets**

As of January 1, 2018 the Group applies IFRS 9 – Financial Instruments, which superseded IAS 39 – Financial Instruments: Recognition and Measurement. The Group chose to apply the standard and the amendment to the standard as of January 1, 2018, without restatement of comparative figures, while adjusting the retained earnings and other equity components to the date of initial application.

The effect of the application of the standard as of the transition day (the date of initial application) is not material.

**1) General**

Financial assets are recognized in the Statement of Financial Position when the Group becomes a party to the contractual terms of the instrument.

Investments in financial assets are recognized for the first time at their fair value, plus transaction costs, with the exception of such financial assets that are classified at fair value through profit and loss, which are recognized for the first time at their fair value. Transaction costs for financial assets at fair value through profit or loss are carried to profit or loss as an immediate expense.

After first-time recognition, financial assets are measured at depreciated cost or fair value, according to their classification.

**Note 2 - Significant accounting policies (Cont.)**

**N. Financial instruments: (Cont.)**

**(1) Financial assets (Cont.)**

**2) Classification of financial assets**

Debt instruments are measured at depreciated cost when the following two conditions are met:

- The Group's business model is to hold the assets with the aim of collecting contractual cash flows, and

- The contractual terms of the asset determine precise dates for receipt of the contractual cash flows that constitute principal and interest payments only.

All other financial assets are measured at fair value through profit and loss.

**3) Financial assets measured at depreciated cost and the effective interest method:**

The depreciated cost of a financial asset is the amount at which the financial asset is measured upon first-time recognition, net of principal payments, plus or net of the aggregate depreciation, while using the effective interest method, of any difference between the initial amount and the payment amount, adjusted for any provision for loss.

The effective interest method is a method used to calculate the depreciated cost of a debt instrument and to allocate and recognize the interest income in profit or loss over the relevant period.

Interest income is calculated using the effective interest method. The calculation is made by applying the effective interest rate to the gross book value of a financial asset, other than:

- For defective financial assets due to credit risk, which were acquired or created, from the date of first-time recognition, the Group applies the effective interest rate adjusted to the credit risk to the depreciated cost of the financial asset.

- For financial assets that are not defective financial assets due to credit risk, that were acquired or created but thereafter became defective financial assets due to credit risk, the Group applies the effective interest rate to the depreciated cost of the financial asset (net of a provision for projected credit losses) in subsequent reporting periods. If, in subsequent reporting periods, the credit risk of the financial instrument improves, such that the financial asset is no longer defective due to credit risk, the Group will calculate the interest income in subsequent reporting periods by applying the effective interest rate to the gross book value.

**Note 2 - Significant accounting policies (Cont.)**

**N. Financial instruments: (Cont.)**

**(1) Financial assets (Cont.)**

**4) Equity instruments designated at fair value through other comprehensive income (see Note 11):**

On the date of first-time recognition, the Group may designate investments in equity instruments, that are not held for trade and do not constitute contingent consideration in a business combination, at fair value through other comprehensive income. This designation cannot be revoked in subsequent periods and can be made for each investment separately, irrespective of the designation or non-designation of other investments at fair value through other comprehensive income.

The Group has investments which were designated thereby on the date of first-time recognition at fair value through other comprehensive income.

On the date of first-time recognition, the investment in equity instruments that were designated at fair value through other comprehensive income is measured at fair value, plus transaction costs. In subsequent periods, the investment is measured at fair value when profits or losses arising from changes in the fair value, including such that derive from changes in exchange rates, are carried to other comprehensive income to a capital reserve for changes in fair value of investments in equity instruments designated at fair value through other comprehensive income and are never reclassified as profit or loss.

Income from dividends in respect of investment in equity instruments designated at fair value through other comprehensive income are recognized in profit or loss when the Group derives the right to receive payments therefor, unless the dividend clearly represents recovery of part of the cost of the investment.

**5) Impairment of financial assets**:

The Group recognizes a provision for projected credit losses in respect of:

- Financial assets measured at amortized cost.
- Contract assets as defined in IFRS 15.

With respect to trade accounts and other receivables, the expected credit losses in respect of such financial assets are assessed based on the Group’s past experience of credit losses and are adjusted for borrower-specific factors, general economic conditions and an estimation of both the current trend of the conditions and the projected trend of the conditions as of the report date, including the time value of money, as needed.

With respect to all other financial instruments, the Group recognizes a provision for impairment according to the projected credit losses throughout the life of the instrument, when there is a significant increase in the credit risk from their date of first-time recognition. If, on the other hand, the credit risk of the financial instrument has not significantly risen from the date of first-time recognition, the Group measures the provision for impairment according to the probability of insolvency in the coming 12 months. The test of whether to recognize a provision for impairment according to the projected credit losses throughout the life of the instrument is based on the risk of default from the date of first-time recognition, and not only when there is objective evidence of impairment on the report date or when the default has actually occurred.

**Note 2 - Significant accounting policies (Cont.)**

**N. Financial instruments: (Cont.)**

**(1) Financial assets (Cont.)**

**5) Impairment of financial assets (Cont.)**

The projected credit losses throughout the life of the instrument are the projected credit losses arising from all possible default events throughout the projected life of a financial instrument. Conversely, projected credit losses in a 12-month period are that part of the projected credit losses throughout the life of the instrument, representing the projected credit losses arising from defaults in a financial instrument that are possible within 12 months after the report date.

In the estimation of the management of the Company, the projected credit losses for customers and contract assets are immaterial.

**Financial asset write-off policy:**

The Group writes off a financial asset when there is information indicating that the borrower is facing severe financial difficulties and there is no realistic chance of recovery of the asset. For example, when the borrower enters dissolution or bankruptcy proceedings. Financial assets that were written off may be subject to enforcement activities in the context of the Group's collection proceedings, while obtaining legal advice as needed. Any recovery of a financial asset that was written off is carried to profit or loss.

**Measurement and recognition of projected credit losses:**

The measurement of projected credit losses is a function of the probability of occurrence of a default, the amount of the loss in the event of occurrence of a default and the maximum exposure to loss in a default event. The estimation of the probability of occurrence of a default and the amount of the loss are based on historic data, adjusted by forward-looking information as described above.

With respect to financial assets, the maximum exposure to a loss in a default event is the gross book value of the financial asset on the report date. With respect to a commitment to give loans and financial guarantee contracts, the maximum exposure to loss in a default event includes the amount taken as of the report date, plus additional amounts that may be incurred in the future until the occurrence of the default based on past data, the Group's knowledge of the specific future financing needs of the borrowers, and other relevant forward-looking information.

With respect to financial assets, projected credit losses are the difference between all the contractual cash flows to which the Group is entitled under the contract, and all the cash flows the Group expects to receive, discounted at the original effective interest rate. With respect to accounts receivable for a lease, the cash flows used to determine the projected credit losses are consistent with the cash flows used to measure the receivable for the lease, in accordance with IAS 17 – Leases.

**Note 2 - Significant accounting policies (Cont.)**

**N. Financial instruments: (Cont.)**

**(1) Financial assets (Cont.)**

**6) Write-off of financial assets**:

The group writes off a financial asset only when the contractual rights to cash flows from the financial asset have expired.

When writing off a financial asset that is measured at depreciated cost, the difference between the book value of the asset and the consideration received or due to be received is recognized in profit or loss.

**(2) Financial liabilities and equity instruments issued by the Group**:

**1) Classification as a financial liability or equity instrument:**

Equity instruments and liabilities issued by the Group are classified as financial liabilities or an equity instrument in accordance with the nature of the contractual arrangements and the definition of financial liability and equity instrument.

**2) Equity instruments**:

An equity instrument is any contract attesting to a residual right in the Group's assets after deduction of all its liabilities. Equity instruments issued by the Group are recorded according to their issue proceeds net of expenses directly related to the issue of such instruments.

**3) Financial liabilities**:

Financial liabilities are stated and measured at depreciated cost.

**Financial liabilities at depreciated cost**

The financial liabilities that are not measured at fair value through profit or loss are recognized for the first time at fair value net of the transaction costs. After the date of first-time recognition, such financial liabilities are measured at depreciated cost while using the effective interest method.

The effective interest method is a method for calculation of the depreciated cost of a financial liability and the allocation of interest expenses over the relevant credit period. The effective interest rate is the rate that accurately deducts the projected future cash flows over the expected life time of the financial liability to its book value or, where applicable, over a shorter period of time.

**4) Write-off of financial liabilities**:

The Group writes off a financial liability when, and only when the financial liability is paid up, cancelled or expires. The difference between the book value of the settled financial liability and the consideration paid is recognized in profit or loss.

**Note 2 - Significant accounting policies (Cont.)**

**N. Financial instruments: (Cont.)**

**(3) Index-linked assets and liabilities that are not measured at fair value**

The value of index-linked financial assets and liabilities, which are not measured at fair value, is revaluated in each period in accordance with the actual rise / fall in the index.

**(4) Deposits from customers**

As part of its business, Supergas receives deposits from its customers in respect of containers and other equipment that are borrowed.

The senior housing residents' deposits are a financial liability with a demand feature and are therefore presented as short-term at the fair value identical to the value of the liability as of the balance sheet date.

The deposits will be returned in accordance with the deposit prices collected by the consolidated companies from their customers, being linked to the index from the day of their latest update. In accordance with IFRS 13, the fair value of financial liabilities with a demand feature is not less than the amount payable on demand, discounted from the first date that the amount could be required to be paid. Accordingly, the deposits are presented at their full value. Moreover, since there is no unconditional right to defer the settlement of the liabilities in respect of the deposits for a period of at least 12 months after the Report Date, and since the customers of the consolidated companies are entitled to demand repayment of the deposit at any time, the deposits are presented as current liabilities, on the basis of their full value.

**O. Fixed assets:**

**(1) Recognition and measurement**

Fixed asset items are measured at cost net of accumulated depreciation and accumulated losses from impairment.

The cost includes expenses that are directly attributable to the acquisition of the asset. The cost of assets that were self-built includes the cost of the materials and the direct labor, as well as any additional cost that is directly attributable to bringing the asset to the location and condition that are required in order for it to operate in the manner intended by management, as well as capitalized credit costs. The cost of purchased software, which constitutes an integral part of the operation of the related equipment, is recognized as part of the cost of such equipment.

Spare parts, servicing equipment and standby equipment are classified as fixed assets when complying with the definition of fixed assets according to IAS 16. Otherwise, they are classified as inventory.

Where significant components of the fixed assets (including significant periodic inspection costs) have a different lifetime, they are accounted as separate items (significant components) of the fixed assets.

A profit or loss from the write-off of a fixed asset item is determined by a comparison of the net consideration from write-off of the asset to the book value, and is recognized in the income statement as other income or other expenses, as the case may be.

**Note 2 - Significant accounting policies (Cont.)**

**O. Fixed assets: (Cont.)**

**(2) Subsequent costs**

The costs of the replacement of a part of a fixed asset item and other subsequent costs, are recognized as part of the book value of such item, if the Group is expected to gain the future economic benefit inherent therein and if its cost can be reliably measured. The book value of the replaced part is written-off. The cost of ongoing maintenance of fixed asset items are carried to the profit and loss as incurred.

**(3) Depreciation**

Depreciation is the systematic allocation of the depreciable amount of an asset over the length of its useful lifetime. The depreciable amount is the cost of the asset, or some other amount that replaces the cost, net of the residual value of the asset.

A depreciated asset, when usable, namely when in the location and condition required in order for it to operate in the manner intended by Management.

Depreciation is carried to the income statement in accordance with the straight line method in accordance with an estimate of the useful lifetime of each part of the fixed asset items, since this method reflects the manner of the forecast consumption of the future economic benefits that are inherent in an asset in the best way. Assets leased under finance leases, including lands, are amortized over the shorter of the lease period and the period in which the assets are used, unless it is reasonably expected that the Group shall acquire ownership over the asset at the end of the lease period. Lands under ownership are not amortized.

**The estimated useful lifetime for the current period and for the comparative periods are as follows:**

| | Useful lifetime in years | Depreciation rate % |
|---|---|---|
| Buildings | 10-50 (primarily 25-50) | 2-10 (primarily 2-4) |
| Plant and equipment | 3-30 (primarily 6-10) | 3-33 (primarily 10-15) |
| Office furniture and equipment | 3-17 | 6-33 |
| Motor vehicles | 5-6 | 15-20 |
| Computers | 3-5 | 20-33 |
| Leasehold installments and improvements | Throughout the lease period, which does not exceed the economic lifetime of the asset. | |

The estimates regarding the depreciation method, useful life and the residual value are reexamined at least in the end of each year and are adjusted when necessary.

**Note 2 - Significant accounting policies (Cont.)**

**P. Investment property:**

Investment property is property (land or a building – or part of a building - or both of them), which is held by the Group for the purpose of the production of rent or for the purposes of a capital gain or both, and not for the purposes of use in the production or supply of goods or services or for administrative purposes or for sale in the ordinary course of business. Investment property, as aforesaid, also includes investment property that is under construction or development.

The Group's investment property includes buildings and land that is owned or held under finance lease, as well as rights in real estate that are held by the Group under operating leasing where otherwise the definition of investment property would be complied with. Investment property is initially measured at cost, which includes transaction costs. In periods following the initial recognition, investment property is measured at fair value. Gains or losses deriving from changes in the fair value of investment property, and with respect to a specific property also those that originate from changes in exchange rates, are recorded in the income statement in the period in which they were generated, under the ‘net profit from adjustment to fair value of investment property and investment property under construction’ item.

Investment property, as aforesaid, also includes investment property that is under construction or development. Investment property under construction is measured at fair value when the value thereof can be reliably measured. Costs of credit are capitalized to investment property under construction. When the fair value cannot be reliably measured, investment property under construction is measured according to cost in the construction period until the earlier of the date of completion of the construction and the date on which the fair value can be reliably measured.

The direct costs of the disposition of investment property are carried to the income statement at the time at which the asset is sold and are setoff against the gain on disposition. The difference between the consideration that is received on the disposition of investment property and the fair value, is the capital gain (loss) on disposition, which is carried to the income statement at the time of the completion of the disposition transaction under "net profit from adjustment to fair value of investment property and investment property under construction".

**Q. Credit costs:**

Specific credit costs and non-specific credit costs are capitalized to qualifying assets and investment property under construction in the course of the period that is required for the completion and for the construction up to the time at which they are ready for their designated use. Non-specific credit costs are capitalized in the same manner for the same investment in qualifying assets and investment property under construction or to the part of it that is not financed by specific credit, using a rate which is a weighted average of the rates of the cost in respect of the sources of credit whose cost has not been capitalized in a specific manner.

All other credit costs are carried to the income statement as incurred.

In the cash flow statement the Group classifies cash flows for interest payments which are capitalized on qualified assets as cash flows used for financing activity, in a manner that is consistent with the Group's policy regarding interest payments in the cash flow statement, as stated in Note 2AA.

**Note 2 - Significant accounting policies (Cont.)**

**R. Intangible assets, except for goodwill:**

Intangible assets are non-financial assets that are not identifiable and which lack a physical presence. Intangible assets having an indefinite useful lifetime are not amortized and are tested for impairment once a year, or at any time at which a sign exists, which indicates the possibility that an impairment has occurred in accordance with the provisions of IAS 36. The estimate of the useful lifetimes of intangible assets having an indefinite lifetime is tested at the end of each reporting year. A change in the estimated useful lifetime of an intangible asset, which turns from being indefinite to being defined is treated by way of "prospective application".

Intangible assets having a defined useful lifetime are amortized on a straight line over the length of their estimated useful lives, subject to testing for impairment. A change in an estimate of the useful lifetime of an intangible asset with a defined lifetime is treated by way of "prospective application".

On the accounting treatment of goodwill - see Note 2J.

**The useful lifetime that have been used in the amortization of intangible assets having a defined lifetime are as follows:**

| | | |
|---|---|---|
| Distribution rights | - | 20 years or according to the term of the agreement, whichever is shorter. |
| Software | - | 3-6 years. |
| Franchise arrangement | | Over the period of the franchise. |
| Others | - | Over the period of the benefit. |

**Intangible assets that were acquired in business combinations**

Intangible assets that were acquired in business combinations are recognized separately from goodwill, where they meet the definition of an asset and identifiable. Intangible assets are identifiable when they are separable or deriving from contractual or other legal rights. Such intangible assets will be recognized at the time of the business combination at their fair value.

In the periods following the initial recognition, intangible assets that have been acquired within the framework of business combinations are presented in accordance with their cost, net of amortization and accumulated losses from impairment. The amortization of intangible assets, having a defined lifetime, is calculated on the straight line basis over the length of their estimated useful lifetimes. The estimate of the useful lifetime and the method of amortization are tested at the end of each reporting year, where the effect of a change in them is treated by way of "prospective application".

**Note 2 - Significant accounting policies (Cont.)**

**S. Leased assets:**

**(1)** Leases, including leases of land from the Israel Land Administration or from other third parties where the Group bears significantly all of the risks and the yields that derive from the asset, are classified as finance leases. On initial recognition, the leased assets are measured, and a liability recognized, in an amount that is equivalent to the lower of the fair value and the present value of the minimum future lease payments. Future payments for exercise of the option to extend the lease period vis-à-vis the Israel Land Administration are not recognized as part of the relevant asset and liability, since they constitute conditioned long-term rent, which derives from the fair value of the land on the future dates of renewal of the lease agreement. Following the initial recognition, the asset is treated in accordance with the accounting policy that is customary in respect of that asset.

The other leases are classified as operating leases, except for leases of real estate that is classified as an investment property, where the leased assets are not recognized in the Group's Statement of Financial Position. Real properties under operating lease, which have been classified by the Group as an investment property, are recognized in the Group's Statement of Financial Position at their fair value, and the lease is accounted as finance lease.

The lease period and the amounts of the amortization take into account any option to extend the lease period, in the event that at the time of the commitment under the lease it is reasonably certain that the option will be exercised.

In a lease of land and buildings the components of the land and the buildings are examined separately for lease classification purposes, with a significant consideration in the classification of the components of the land being the fact that land usually has an indefinite lifetime.

**(2) Lease payments**

Payments in the framework of an operational lease are carried to the income statement using the straight line method throughout the lease period.

On the publication of a new standard on leases, IFRS 16 “Leases” – see Note 2DD.

**Note 2 - Significant accounting policies (Cont.)**

**T. Inventory:**

Inventory is an asset held for the purpose of sale in the ordinary course of business, in a production process for the purpose of sale or materials to be consumed during the production process or during the delivery of the services.

**(1) Inventory of gas**

Inventory is presented at the lower of its cost and net realizable value. The cost of the inventory of gas is calculated on the basis of "first in first out" (FIFO), and it includes the costs of the acquisition of the inventory and of bringing it to its current location and condition.

The cost of inventory of devices and parts, spare parts and materials for installations is calculated according to the moving average method.

**(2) Azrieli E-commerce product inventory**

Inventory is presented at the lower of its cost and net realizable value. The cost of inventory includes all acquisition costs.

Net realizable value represents the estimated selling price in the ordinary course of business, net of an estimate of the costs for completion and an estimate of the costs required to carry out the sale.

The cost is calculated on the basis of "first in first out" (FIFO).

**(3) Other inventory**

Is presented at the lower of its cost and net realizable value. The cost of inventory is determined primarily on the “moving average” basis.

**U. Impairment of non-financial assets:**

At the end of each reporting period, the Group tests whether any signs whatsoever exist, which evidence an impairment of its tangible and intangible assets, other than inventory. In the event that signs exist, as aforesaid, an estimate is made of the recoverable amount of the asset, with the objective of determining the amount of the loss from impairment that has arisen, if any. Where it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the cash generating unit to which the asset belongs. Common assets are also allocated to the individual cash generating units in the event that it is possible to identify a reasonable and consistent basis for such an allocation.. In the event that it is not possible to allocate the common assets to the individual cash generating units on the said basis, the common assets are allocated to the smallest cash generating units in respect of which it is possible to identify a reasonable and consistent basis for the allocation.

A recoverable amount is the higher of the fair value of an asset net of sale costs and its value in use. In the evaluation of the value in use, estimated future cash flows are discounted to their present value, using a pre-tax discount rate, which reflects the market's present evaluation in respect of the time value of the money, and the specific risks that relate to the asset, in respect of which the estimated future cash flows have not been adjusted.

Where the recoverable amount of an asset (or of a cash generating unit) is estimated to be lower that the carrying value, the book value of the asset (or of the cash generating unit) is written down to its recoverable amount. A loss from impairment is recognized immediately as an expense in the income statement, unless the relevant asset is measured in accordance with the revaluation model. In that case, the loss from impairment is treated as a reduction of the revaluation reserve, until it is reduced to zero, and the balance of the reduction, if there is one, is recognized in the income statement.

**Note 2 - Significant accounting policies (Cont.)**

**U. Impairment of non-financial assets: (Cont.)**

Where a loss from impairment that has been recognized in previous periods is cancelled, the book value of the asset (or of the cash generating unit) is increased back to the updated estimated recoverable amount, but not more than the book value of the asset (or of the cash generating unit) that would have been set if it were not for the recognition of a loss from impairment in respect of its in previous periods. The cancellation of a loss from impairment is recognized immediately in the profit and loss.

**V. Provisions:**

A provision is recognized where the Group has a current commitment, whether legal or implicit, as the result of an event that has taken place in the past, which can be reliably measured, and where it is expected that economic resources will be required in order to clear the commitment.

**(1) Legal claims**

A provision for claims is recognized where the Group has a present legal commitment or an implicit commitment as the result of an event that has taken place in the past, it being more likely than not that the Group will be required to use economic resources to settle the commitment and it may be reliably estimated. Where the impact of the time value is material, the provision is measured in accordance with its present value.

**(2) Warranty**

A provision for warranty is recognized when the products or the services for which the liability is provided, are sold. The provision is based on historic data and also on assessments of the management and the weighting all the possible outcomes by their probabilities.

**W. Revenues:**

**(1) Rent income**

Rent income in respect of investment property is recognized on the straight line basis over the length of the relevant rent period.

In operating lease arrangements in which in the beginning of the lease period no rent is received, or reduced rent is received, and when additional benefits are given to the lessee, the Group recognizes revenue on a straight line basis, over the lease period.

**(2) Revenue from contracts with customers in Granite Group companies** (“**Granite**”)

Starting from January 1, 2018, Granite has for the first time been applying International Financial Reporting Standard 15 (in this section, “**IFRS 15**” or the “**Standard**”) which sets forth guidelines with respect to the recognition of revenue. The effect of the change in the Standard as of the transition date (the date of initial application) is immaterial.

The Standard presents a new model for recognizing revenue from contracts with customers which includes five phases:

(1) Identification of the contract with the customer.
(2) Identification of distinct performance obligations in the contract.
(3) Determination of the transaction price.
(4) Allocation of the transaction price to distinct performance obligations.
(5) Recognition of the revenue upon satisfaction of the performance obligations.

**Note 2 - Significant accounting policies (Cont.)**

**W. Revenues: (Cont.)**

**(2) Revenue from contracts with customers in Granite Group companies ("Granite") (Cont.)**

Granite recognizes revenue when the customer obtains control over the promised goods or service. The revenue is measured according to the consideration amount to which the Group expects to be entitled in consideration for the transfer of goods or services that were promised to the customer, other than amounts collected in favor of third parties, if any.

In the context of the initial application of the Standard, Granite elected to implement the relief of application of the cumulative effect approach only for contracts not yet ended as of the transition date.

Granite recognizes revenue when the customer obtains control over the promised goods or service. The revenue is measured according to the consideration amount to which Granite expects to be entitled in consideration for the transfer of goods or services that were promised to the customer, other than amounts collected for the benefit of third parties.

According to the new Standard, the accounting treatment of incremental costs of obtaining a contract with the customer will be recognized as an asset, and Granite's management believes that the Group is expected to recover such costs.

Accordingly, incremental costs incurred by Granite in relation to the construction of infrastructures for central gas customers shall be recognized as an asset ("**Contract Fulfillment Costs**") and amortized on a systematic basis in profit or loss.

Furthermore, according to the Standard, revenue from gas system infrastructure connection fees, which grant the customer a material right in relation to the renewal of the contract ("**Contract Liability**"), will be recognized as a liability and allocated over the expected life of the contract with the customer *in lieu* of recognition as immediate revenue in the income statement.

As stated above, on the transition date, a relief that is allowed by the Standard was applied, whereby adjustment of revenue for agreements that ended as of the transition date will not be included. Granite's contracts with the central gas customers, which are renewed on a monthly basis and may be terminated by the customer at any point in time with no exit penalty, are contracts that had ended as of the date of initial application of the Standard.

**Contract identification**

Granite treats a contract with a customer only when all of the following conditions are met:

**(a)** The parties to the contract have confirmed the contract (in writing, orally or according to other prevailing business practices) and are committed to satisfying the obligations attributed to them;

**(b)** Granite is able to identify the rights of each party with regard to the products or services to be provided;

**(c)** Granite is able to identify the terms of payment for the goods or services to be provided;

**(d)** The contract is of a commercial nature (i.e. the risk, timing and amount of the entity's future cash flows are expected to change as a result of the contract); and

**(e)** Granite is expected to collect the consideration to which it is entitled for the goods or services to be provided to the customer.

**Note 2 - Significant accounting policies (Cont.)**

**W. Revenues: (Cont.)**

**(2) Revenue from contracts with customers in Granite Group companies ("Granite") (Cont.)**

In order to comply with Section (e) Granite examines, *inter alia*, the rate of the advance payments that were received and the installment payment arrangement in the contract, previous experience with the customer and his condition and the existence of adequate guaranties.

When a contract with a customer does not fulfill the aforesaid criteria, consideration received from the customer is recognized as a liability until the criteria are fulfilled or one of the following events occurs: Granite no longer has obligations to provide goods or services to the customer and all of the consideration promised by the customer has been received and is non-refundable; or, the contract was terminated and the consideration that has been received from the customer is non-refundable.

**Identification of performance obligations**

On the date of the engagement in the contract, Granite assesses the goods or services that were promised in the context of a contract with a customer and identifies as a performance obligation any promise to provide the customer with one of the following two:

(a) Goods or a service (or a package of goods or services) that are separate; or

(b) A set of separate services or goods that are *de facto* identical and have the same pattern of provision to the customer.

Granite identifies goods or services that were promised to the customer as separate when the customer is able to derive benefit from the goods or service alone or together with other resources that the customer can easily obtain, and Granite's promise to provide the goods or service to the customer can be identified separately from other promises in the contract. In order to examine whether a promise to provide goods or a service is identifiable separately, Granite examines whether a significant service is rendered for combining the goods or service with other goods or services that were promised in the contract into a combined product for which the customer engaged in the contract.

In the field of LPG supply, Supergas identified one performance obligation in each contract.

In the field of natural gas supply, Supergas identified two separate performance obligations – gas conversion and natural gas supply.

In the field of franchises GES identified two separate performance obligations: rendering of construction services and rendering of operating services.

**Determination of the transaction price**

The transaction price is the amount of the consideration to which Granite expects to be entitled in consideration for the provision of goods or services that were promised to the customer, other than amounts collected for the benefit of third parties. At the time of determining the transaction price Granite takes into account the effect of all of the following: variable consideration, existence of a significant financing component in the contract, non-cash consideration and consideration payable to the customer.

**Note 2 - Significant accounting policies (Cont.)**

**W. Revenues: (Cont.)**

**(2) Revenue from contracts with customers in Granite Group companies ("Granite") (Cont.)**

**Variable consideration**

The transaction price includes fixed amounts and amounts that may change as a result of discounts, refunds, credits, price concessions, incentives, performance bonuses, fines, claims and disputes and changes to the contract, the consideration for which has not yet been agreed between the parties.

In the transaction price Granite includes the amount of the variable consideration, or part thereof, only when there is a high level of expectancy that significant cancellation of the amount of the cumulative revenue that was recognized will not occur when the uncertainty related to the variable consideration will be clarified thereafter. At the end of each reporting period, Granite updates, insofar as necessary, the estimate of the variable consideration amount that is included in the consideration for the transaction.

In construction contracting, variable consideration chiefly derives from deviations in quantity and performance, penalties for delays and bonuses for early performance.

Granite assesses the variable consideration amount by estimating the most likely amount that will be received, as this method best describes the amount of the consideration to which it will be entitled.

**The existence of a significant financing component**

In order to measure the transaction price, Granite adjusts the amount of the consideration promised due to effects of the time value of the money if the timing of the installments that was agreed between the parties, gives the customer or Granite a significant financing benefit. In such cases, the contract contains a significant financing component. In assessing whether a contract contains a significant financing component, Granite examines, *inter alia*, the forecast period of time between the date on which Granite provides the goods or services that were promised to the customer and the date on which the customer pays for such goods or services and the difference, if any, between the amount of the consideration that was promised and the cash sale price of the promised goods or services.

When the contract contains a significant financing component, Granite recognizes the consideration amount while using the capitalization rate that will be reflected in a separate financing transaction between it and the customer on the engagement date. The financing component is recognized as revenue or as interest expenses in the period that are calculated in accordance with the effective interest method.

In cases where the difference between the date of receipt of the payment and the date of provision of the goods or service to the customer is one year or less, Granite applies the practical relaxation set forth in the Standard and does not separate a significant financing component.

**Satisfaction of a performance obligation**

Revenue is recognized when Granite satisfies a performance obligation by transferring control over goods or a service that were promised to the customer.

For supply of LPG and natural gas, the customer obtains control upon the supply of the gas and therefore Supergas recognizes the revenue on such date.

**Note 2 - Significant accounting policies (Cont.)**

**W. Revenues: (Cont.)**

**(2) Revenue from contracts with customers in Granite Group companies ("Granite") (Cont.)**

**Satisfaction of a performance obligation (Cont.)**

For conversion of gas systems, Supergas transfers control over time and therefore recognizes revenue over time, as the performance of Supergas creates or improves an asset that is controlled by the customer while it is being created or improved.

In the field of construction contracting, GES transfers control over time and therefore recognizes revenue over time, as the performance of the Group creates or improves an asset that is controlled by the customer while it is being created or improved.

For franchise operation services – revenue is recognized over time in the report period in which the services were provided since the customer concurrently receives and consumes the benefits provided by the performance of GES while GES provides the aforesaid services.

**Measurement of progress in satisfying a performance obligation**

Granite recognizes revenue over time by measuring the progress toward full satisfaction of the performance obligation in such manner that reflects Granite's performance in the transfer of control over the goods or services that were promised to the customer. When it is not possible to reasonably measure the result of a performance obligation (for example, in the early stages of a contract) but Granite expects to recover the costs that were incurred, revenue is recognized only up to the amount of the costs that were incurred (zero margin) until such date as the result of the performance obligation can be reasonably measured.

**Granite measures the progress through an input-based method**

In accordance with the aforesaid method, the completion rate is determined based on an estimate of the total costs required to complete the performance obligation. The aforesaid estimate includes the direct costs and indirect costs that directly refer to the satisfaction of the performance obligation and are allocated based on reasonable attribution. In Granite's opinion, using the cost method presents, in the most appropriate way, the manner of transfer of the control to the customer.

Upon applying an input-based approach, Granite does not include the effect of any input that does not reflect Granite's performance in the transfer of the control over the goods or services to the customer.

Upon measuring the progress of the performance through an input-based method, cost that was incurred which is disproportionate to progress in the satisfaction of a performance obligation is not taken into account in measuring the completion rate. In such cases, Granite recognizes revenue in an amount that is equal to the cost of goods used to satisfy the performance obligation (i.e., zero margin), when all of the following conditions are met: the goods are not separate; the forecast is that the customer will obtain control over the goods a significant time before receipt of the respective services; the cost of the goods is significant relative to the total projected contract costs; and Granite is purchasing the goods from a third party and is not significantly involved in the design and manufacture of the goods.

## Note 2 - Significant accounting policies (Cont.)

### W. Revenues: (Cont.)

#### (2) Revenue from contracts with customers in Granite Group companies ("Granite") (Cont.)

**Contract changes**

A change to the contract is a change in the applicability or price (or both) of a contract that was confirmed by the parties to the contract. A contract change can also be confirmed in writing, in an oral agreement or implied by prevailing business practices. A contract change can also occur in cases where the parties to the contract disagree with regard to the applicability or price (or both) of the change or when the parties confirmed the change to the applicability of the contract but have yet to determine the parallel price change.

In cases where the change to the contract has not yet been confirmed by the parties, Granite continues to recognize revenue pursuant to the existing contract, irrespective of the contract change, until such date as the contract change is confirmed or legally enforceable.

Granite treats a contract change as an adjustment of the existing contract since the remaining goods or services subsequently to the contract change are not separate and therefore constitute part of one performance obligation that is partially satisfied on the contract change date. The effect of the change on the transaction price and on the extent of the progress toward full satisfaction of the performance obligation is recognized as a revenue adjustment (increase or decrease) on the contract change date, i.e. on a catch-up basis.

**Contract asset and contract liability**

A contract asset is recognized when Granite has the right to consideration for goods or services that Granite provided to the customer, such right being contingent on a factor other than the lapse of time for example, on Granite's future performance. The contract assets are classified to the receivables item when the rights to receive the same become non-contingent.

A contract liability is recognized when Granite is obligated to provide a customer with goods or services for which it received consideration from the customer (or the amount is due and payable).

**Setoff of a contract asset and a contract liability**

An asset and a liability due to the same contract are presented, net, in the statement of financial position. However, a contract asset and liability that derive from different contracts are presented, gross, in the statement of financial position.

#### (3) Income from management and maintenance fees and net income from the use of electricity

Income from management and maintenance fees and net income from the use of electricity is reflected pro-rata over the length of the period in which the relevant services are provided.

#### (4) Dividend income

Income from dividends in respect of investment in equity instruments designated at fair value through other comprehensive income are recognized in profit or loss when the Group derives the right to receive payments therefor, unless the dividend clearly represents recovery of part of the cost of the investment.

**Note 2 - Significant accounting policies (Cont.)**

**W. Revenues: (Cont.)**

**(5) Senior housing revenues**

(1) The revenues from management and maintenance fees are recorded in the income statement upon performance of the service.

(2) The revenues from forfeiture of deposits are recorded in the income statement when created.

**(6) Revenues from provision of senior housing services**

The revenues from provision of services are recorded proportionately over the term of the agreement or upon provision of the service if the likelihood of the flow of the economic benefits attributed to provision of the service is certain.

**X. Franchise arrangements for provision of services:**

The Group engaged, via GES Environmental Solutions Ltd., with authorities from the public sector, to provide BOT (Build, Operate, Transfer) services for construction of facilities, wastewater treatment, and improvement of wells.

In the context of franchise arrangements for the provision of services to public entities for the construction and operation of infrastructure assets in consideration for fixed and variable payments, the Group recognizes a financial asset or an intangible asset, according to the terms and conditions of the arrangement.

The financial asset reflects the unconditional payments that will be received from the public entity, which are not contingent on use of the infrastructure by users and it is measured considering an appropriate risk interest determined according to the risk of the customer and the project. The intangible asset represents the difference between the fair value of the infrastructure assets construction services and the unconditional amount that will be received from the public entity (the aforesaid financial asset), which reflects the right to charge usage fees from the public of users of the facility.

The Group's right to receive the consideration for the construction services, whether under the financial asset model or under the intangible asset model, constitutes a contract asset until the end of the construction period. However, under the intangible asset model, the recognized contract asset will be presented under intangible assets. In projects treated according to the financial asset model, when, at the end of the construction period, the right to receive consideration for the construction services is not contingent (other than on the lapse of time), the contract asset is classified under receivables (financial asset) according to the book value of the contract asset. When, at the end of the construction period, the right to receive consideration for the construction services is contingent on another factor other than the lapse of time (such as the ongoing operation of the infrastructure), the contract asset is not reclassified until the right to receive the consideration is non-contingent, which means, in certain project, classification as a contract asset until the date of actual receipt of the consideration.

If the payment received by the Group for the construction services is partly comprised of a financial asset and partly comprised of an intangible asset, the Group treats every component of the consideration separately. The consideration received or due for both of the components is recognized initially at fair value.

**Note 2 - Significant accounting policies (Cont.)**

**Y. Taxes on income:**

**(1) General**

Tax expenses (income) on income include the sum of the current tax as well as the change in the deferred tax balances, except in respect of deferred taxes that derive from transactions that are reflected directly under shareholders' equity.

**(2) Current taxes**

The current tax on income expenses is calculated based on the Company and the consolidated companies' chargeable income for tax purposes, during the course of the reporting period. The chargeable income is different from the income before taxes on income, as the result of the inclusion or the non-inclusion of income and expense items that are chargeable to taxation or which are allowable as a deduction in different reporting periods, or which are not chargeable to tax or allowable as a deduction. Current tax assets and liabilities have been calculated on the basis of the tax rates and the tax laws that have been legislated or whose legislation has been effectively completed as of the date of the Statement of Financial Position.

A provision for uncertain tax positions including additional tax and interest expenses, is recognized when it is more likely than not that the Group will resort to its financial resources to settle the liability.

Current tax assets and liabilities are presented as offset, where the entity has an enforceable legal right to offset the amounts recognized as well as an intention to settle on a net basis, or to realize the asset and settle the liability at the same time.

**(3) Deferred taxes**

The companies in the Group record deferred taxes in respect of timing differences between the values of assets and liabilities for tax purposes and their values in the Financial Statements. Deferred tax balances (assets or liabilities) are calculated in accordance with the tax rates that are expected to apply at the time that they are realized, based on the tax rates and the tax laws that have been legislated or whose legislation has been effectively completed as of the date of the Statement of Financial Position. Deferred tax liabilities are generally recognized in respect of all of the temporary differences between the value of assets and liabilities for tax purposes and their values in the Financial Statements. Deferred tax assets are recognized in respect of temporary differences that can be deducted up to the amount of the chargeable income against which it is expected that the deductible temporary differences can be exploited. The deferred taxes in respect of the structure component of investment property are calculated in accordance with a business model whose purpose is significant consumption over time of all of the economic benefits incorporated therein.

The calculation of the deferred taxes does not take into account the taxes that would have applied in the event of the disposition of the investments in investee companies, since in the Group’s management estimate, the temporary differences which are the subject matter of such deferred taxes are under the control of the Group and are not expected to reverse in the foreseeable future.

Deferred tax assets and liabilities are presented as offset, where the entity has an enforceable legal right to offset current tax asset against current tax liabilities, and where they refer to income taxes that are imposed by such tax authority, and the Group intends to settle the current tax assets and liabilities on a net basis.

**Note 2 - Significant accounting policies (Cont.)**

**Z. Earnings per share:**

The Company calculates the amounts of the basic earnings per share in respect of the profit or loss that is attributable to the shareholders in the Company by dividing the profit or loss that is attributable to the shareholders in the Company by the weighted average number of ordinary shares in circulation during the course of the reporting period.

**AA. Classification of interest paid, dividends paid, interest and dividends received and income taxes paid, net, in cash flow statement:**

The Group classifies cash flows due to interest and dividends received thereby as cash flows from investment activity, as well as cash flows due to interest that was paid as cash flows used for the financing activity. Cash flows due to income taxes are classified in general as cash flows used for operating activities, other than cash flows that are easily identifiable with cash flows used for investment or financing activity. Dividends paid by the Group are classified as cash flows from financing activity.

**BB. Exchange rates and linkage base:**

**(1)** Balances that are stated in foreign currency or which are linked thereto are recorded in the Financial Statements in accordance with the representative exchange rates that were published by the Bank of Israel and which were in force as of the date of the Statement of Financial Position.

**(2)** Balances that are linked to the CPI are presented in accordance with the last known index as of the date of the Statement of Financial Position (the index for the month preceding the date of the Financial Statements), or in accordance with the index in respect of the last month of the reporting period (the index for the month in which the date of the Financial Statements lies), in accordance with the terms of the transaction.

**(3) The following are details in respect of the exchange rates and Index:**

| | Representative exchange rate of | | Index in Israel | |
|---|---|---|---|---|
| | Euro NIS to 1 Euro | Dollar NIS to 1 Dollar | Index for Basis 1993 | Known index Basis 1993 |
| **The date of the Financial Statements:** | | | | |
| as of December 31, 2018 | 4.292 | 3.748 | 223.33 | 224.00 |
| as of December 31, 2017 | 4.153 | 3.467 | 221.57 | 221.35 |
| as of December 31, 2016 | 4.044 | 3.845 | 220.68 | 220.68 |
| | % | % | % | % |
| **Rates of change for the year ended:** | | | | |
| December 31, 2018 | 3.35 | 8.10 | 0.80 | 1.20 |
| December 31, 2017 | 2.69 | (9.83) | 0.40 | 0.30 |
| December 31, 2016 | (4.78) | (1.46) | (0.20) | (0.30) |

**Note 2 - Significant accounting policies (Cont.)**

**CC. New amendments, new interpretations and amendments to standards that affect the current period and/or previous reporting periods**

- **International Financial Reporting Standard (2014) IFRS 9 – Financial Instruments** – See details in Section 2N.

- **International Financial Reporting Standard IFRS 15 – Revenue from Contracts with Customers** – See details in Section 2W(2).

- **Amendment IAS 40 "Investment Property" (regarding transfers from/to investment property)**:

  The amendment clarifies the provisions on transition from/to investment property with an emphasis on whether property under construction that was initially classified as inventory can be reclassified as investment property. The amendment emphasizes that a reclassification will only be made where there is evidence of a change in the use of the property. A change in management's intentions regarding the use of the property, in itself, is insufficient as evidence of change of use. It was also emphasized that the evidence items specified in the standard are merely examples and are not a closed list.

  The amendment is implemented by the method of prospective application for annual reporting periods beginning on January 1, 2018 or thereafter.

**DD. Standards, interpretation and amendments to standards that were released and are not in effect, and were not pre-adopted by the Group, that have or may have an effect on future periods:**

**IFRS 16 "Leases":**

The new standard cancels IAS17 "Leases" and the commentaries related thereto, and sets forth the rules for recognition, measurement, presentation, and disclosure of leases with regards to both of the parties to the transaction, i.e. the customer ("**Lessee**") and the supplier ("**Lessor**"). The standard does not change the currently existing accounting treatment in the Lessor's books.

The new standard cancels the currently existing distinction relating to a Lessee, between finance leases and operating leases and determines a uniform accounting model with regards to all types of leases. In accordance with the new model, for any leased asset, the lessee is required on the one hand to recognize an asset for the right of use and on the other hand, a financial liability for the lease payment.

The directives on the recognition of an asset and liability, as aforesaid, shall not apply to assets which are leased for a term of up to 12 months only, and to leases of low value assets (such as personal computers).

In view thereof, leases of the Group that are currently treated as operating leases will be recognized upon the implementation of the standard as assets and liabilities in the Group's statement of financial position.

The standard takes binding effect for the annual reporting periods which commence on January 1, 2019, or thereafter.

The Group intends not to apply the requirements of recognition of a right-of-use asset and a liability to leases the lease term of which expires within 12 months of the date of initial application.

**Note 2 - Significant accounting policies (Cont.)**

**DD. Standards, interpretation and amendments to standards that were released and are not in effect, and were not pre-adopted by the Group, that have or may have an effect on future periods: (Cont.)**

Furthermore, the nominal discount rates used to measure the lease liability range between 2.65% and 4.8%. Such range is affected by differences in the duration of the leases, a difference in the various asset groups, a change between the discount rates of the Group’s companies.

The application of the standard is not expected to have a material effect on the financial statements.

**Note 3 - Critical estimates and the determination of the fair value**

**A. General:**

In the implementation of the Group's accounting policy, which is described in Note 2 above, the managements of the companies in the Group are required to exercise broad accounting judgment in respect of estimates and assumptions, in connection with the carrying values of assets and liabilities, which cannot necessarily be found in other sources. The estimates and the related assumption are based on past experience and on other factors, which are considered to be relevant. The actual results may well be different from those estimates.

The estimates and assumptions that they are based on are reviewed routinely by the management of the companies in the Group. Changes in the accounting estimates are recognized only in the period in which the change is made in the estimates in the event that a change affects only one period or they are recognized in the said period and also in future periods in cases where the change affect both the current period and also the future periods.

**B. Critical estimates:**

Following is information in respect of critical estimates, which have been prepared whilst implementing the accounting policies, and which have a significant impact on the Financial Statements:

**(1)** The revaluation of investment property and investment property under construction – (see Notes 3C(1), 13 and 34) in accordance with the IFRS and in accordance with the Company’s selection, the Group presents investment property and investment property under construction in accordance with the fair value, based mainly on an evaluation by independent external appraisers, possessing the appropriate professional skills.

The fair value is examined at least once a year and at any time at which indications exist that there has been a significant change in value. Even in the case where the indications do not exist, the Company’s management may, per its discretion, choose to perform valuations. In each case where the Company’s management decides to update the fair value of all or part of the assets, as the case may be, the BOD report for such quarter shall include the Board's explanations in respect of the valuation that it made itself, as required by law.

Changes in the fair value are carried to the income statement and accordingly they may have a material effect on the Company's results.

**(2)** Contingent liabilities (see Note 31) – in the evaluation of the chances of the legal claims that have been filed against the Company, its consolidated companies and associates, the companies have relied on the opinions of their legal counsel as well as on estimates made by their managements. These evaluations by the legal counsel and the managements are based on their best professional judgment, taking into account the stage at which the proceedings are to be found, and also on the legal experience that has accumulated on various subjects. Since the results of the claims will be determined in the courts, those results may be different from those evaluations.

## Note 3 - Critical estimates and the determination of the fair value (Cont.)

### C. Determination of fair value:

As part of the accounting principles and the disclosure requirements, the Group is required to determine the fair value of non-financial and financial assets and liabilities. The fair values have been determined for the purposes of measurement and/or disclosure on the basis of the methods that are described below. Additional information in respect of the assumptions that have been used in the determination of the fair value is provided in the noted that relate to this asset or liability.

**(1)** Investment property and investment property under construction – As aforesaid in Note 2P, the Group's investment property is presented at fair value, where changes in the fair value are carried to the income statement as income or as expenses.

For the purpose of the determination of the fair value of investment property, the Company's management bases itself, primarily, on evaluations that are performed once a year by independent appraisers of land, having the required knowledge, experience and expertise. The Company's management is in the habit of determining the fair value in accordance with generally accepted evaluation methods of real properties, primarily discounted cash flow and comparison with selling prices of similar assets and land and the Group's assets in the near environment. Where use has been made of the discounted cash flow method, the interest rate used in the discounting of the net cash flows that are expected from the asset can have a significant impact on the fair value.

In the determination of the fair value of investment property, the following are taken into account, *inter alia* and insofar as is relevant: the location of the property and its physical state, the cap rates, the occupancy rates, the tenant turnover rates, selling prices, the quality of the tenants and their stability, the rent period, the rent prices in similar properties, the adjustments that are required to the existing rent prices, the actual and forecast occupancy levels for the property and the costs of operating it. In the determination of the fair value of investment property under construction, the following are taken into account, *inter alia* and insofar as is relevant: the duration of the construction of the project, the selling prices, the amount of the rent, the additional cost required for construction thereof until the current operation thereof and the interest rate, the project's risk premium, deduction of developer profit and the required cap rate. In the determination of the fair value of land, the following are taken into account, *inter alia*: the location of the land, the rights and comparative transactions of similar properties, while making the required adjustments. A change in the value of any of these components, or all of them, could have a significant impact on the fair value of the property as estimated by the Company's management.

The Group strives to determine as objective a fair value as possible, but at the same time, the process of estimating the fair value of investment property also includes subjective elements, which are sources, *inter alia*, in the past experience of the Company's management and its understanding of what is expected to take place in the investment property market at the time at which the estimate of the fair value is determined. In the light of what is stated in the previous paragraph, the determination of the fair value of the Group's investment property mandates the exercise of judgment. Changes in the assumptions that were used in the determination of the fair value could have a significant effect on the Group's state of affairs and the results of its activities.

The Company reviews in its quarterly reports the need to update the value of the investment property by examining macro-economic changes that may have a material effect on the fair value of the properties and/or upon the occurrence of a material event in an asset that was defined as a material or a very material asset in the Company's statements, due to population, material change in rent, etc. Also, with regard to investment property under construction, the following are taken into account: the costs actually invested during the period, the updated forecast of costs for completion and lease agreements signed during the period. Upon initial classification of a property that was under construction as investment property, and insofar as no valuation was received therefor in the six months preceding the classification date, an external valuation will be performed therefor, as of the end of the quarter in which it was first classified as investment property.

**Note 3 - Critical estimates and the determination of the fair value (Cont.)**

**C. Determination of fair value (Cont.)**

**(2)** Impairment of goodwill – in order to determine whether an impairment has taken place in the value of goodwill, the Company's management prepares an estimate of the value in use of the cash generating units to which the goodwill has been allocated, for the purpose of the calculation of the value in use, the Group calculates an estimate of the future cash flows that are expected to derive from each of the cash generating units as well as the appropriate discount rate in order to calculate the present value.

**(3)** Investments in shares – the fair value, net of sale costs, of financial assets (mainly investment in Bank Leumi) is determined whilst relating to their average quoted closing bid prices at the reporting date.

**(4)** Loans and receivables including trade and other receivables – the fair value of loans and receivables including trade and other receivables, except for construction works in progress, but including receivables in respect of franchise arrangements, is determined on the basis of the current value of the future cash flow, discounted at the market interest rate, which takes into account, inter alia, the risk of the borrower as of the measurement date. Short term trade and other receivables without a stated interest rate, are measured at the original invoice amount, if the discounting effect is immaterial. The fair value of loans and receivables is determined on the initial recognition date. In the periods following the initial recognition date, the fair value is calculated solely for the purposes of providing disclosure.

**Note 4 - Cash and cash equivalents and short-term deposits and investments**

**A. Composition of cash and cash equivalents:**

| | As of December 31 | |
|---|---|---|
| | **2018** | **2017** |
| | **NIS in millions** | **NIS in millions** |
| Balances with banks | 283 | 210 |
| Short-term deposits – in NIS unlinked | 358 | 778 |
| Short-term deposits – in dollars | 55 | 27 |
| Financial funds | 20 | 49 |
| **Total cash and cash equivalents** | 716 | 1,064 |

**B. Short-term deposits and investments:**

As of December 31, 2018, the item includes short-term deposits of more than 3 months and a deposit in the sum of approx. NIS 38 million which is deposited in a special account as stated in Note 19B(5), with interest at the range of 0.01%-1.2% (as of December 31, 2017 – NIS 37 million with interest at the range of 0.01%-1.2%).

## Note 5 - Trade accounts receivable

**The composition:**

| | As of December 31 | |
|---|---|---|
| | 2018 | 2017 |
| | NIS in millions | NIS in millions |
| Open debts | 328 | 267 |
| Income receivable | 31 | 31 |
| | 359 | 298 |
| Net of – provision for doubtful debts | (17) | (13) |
| | 342 | 285 |

For details regarding the credit risk management by the Group – see Note 32B.

## Note 6 - Other receivables

**The composition:**

| | As of December 31 | |
|---|---|---|
| | 2018 | 2017 |
| | NIS in millions | NIS in millions |
| Institutions | 21 | 35 |
| Pre-paid expenses | 25 | 23 |
| Deposits in trust | 47 | 54 |
| Advance payments to suppliers | 3 | 2 |
| Current maturities of receivables in respect of franchise arrangement | 5 | 5 |
| Receivables for work in progress | 3 | 8 |
| Accounts receivable | 8 | 10 |
| Insurance indemnity receivable (*) | 23 | 68 |
| Other receivables | 24 | 21 |
| | 159 | 226 |

(*) See Note13D(1).

## Note 7 - Inventory

**The composition:**

| | As of December 31 | |
|---|---|---|
| | 2018 | 2017 |
| | NIS in millions | NIS in millions |
| Raw materials | 5 | 3 |
| Work in progress | - | 9 |
| Finished works | 53 | 43 |
| Servicing material, spare parts and installations | 8 | 9 |
| | 66 | 64 |

## Note 8 – Discontinued operations

On April 14, 2016, Granite Hacarmel entered into an agreement with Israel Oil Gas Fund L.P., a limited partnership incorporated in Israel the general partner of which controlled by Mr. David Weissman (the "**Buyer**") for the sale of all of Granite Hacarmel's holdings (100%) in Sonol Israel Ltd. (the "**Agreement**" and "**Sonol**", respectively). On July 24, 2016, the transaction was closed.

The total consideration amounts to NIS 363.5 million, of which NIS 187.5 million was paid in cash upon the closing of the transaction (subject to certain adjustments determined in the Agreement); a sum of NIS 21 million of the consideration was paid in cash within 18 months of the closing date; a sum of NIS 52.5 million was deducted from the consideration against dividends that were distributed by Sonol up to the closing of the transaction, and a sum of NIS 5 million will be paid against the repayment of certain debts of Sonol's debtors.

Of the consideration, a sum of NIS 97.5 million was paid at the closing date through the assumption of a liability of the Buyer to repay a loan that is secured by a charge on all of the sold shares. The loan will bear an annual interest comprising Prime interest + 1% and shall be paid on a quarterly basis (the "**Loan**"). The principal of the Loan shall be paid in one installment within 60 months of the transaction closing date. To secure the repayment of the Loan, the Buyer undertook (1) not to effect distributions, as defined in the Companies Law, until the full repayment of the Loan (principal and interest), unless certain cumulative conditions agreed by the parties shall have been fulfilled; and (2) compliance with limitations on changes of control in the Buyer. The principal of the Loan was repaid in installments and as of the date of the Statement of Financial Position, the principal of the Loan is in the sum of NIS 75 million.

The transaction did not include Pi Glilot's lands and the shares of Pi Glilot Oil and Pipe Terminals Co. Ltd. For additional details see Note 11C.

In accordance with the provisions of IFRS 5 "Non-current Assets Held for Sale and Discontinued Operations", Sonol's results are presented separately in the income statement as discontinued operations and comparative figures in the income statement have been restated according to Section 34 of IFRS 5.

## Note 8 – Discontinued operations (Cont.)

**Set forth below are the results attributed to the discontinued operations:**

| | As of the year ended December 31 | | |
|---|---|---|---|
| | 2018 | 2017 | 2016 |
| | NIS in millions | NIS in millions | NIS in millions |
| **Results of the discontinued operations** | | | |
| Revenues | - | - | 1,596 |
| Expenses | - | - | 1,590 |
| **Income before income taxes** | - | - | 6 |
| Income taxes | - | - | 9 |
| **Loss after income taxes** | - | - | (3) |
| Sale costs and expenses | - | - | (5) |
| Loss from sale of discontinued operations, net of tax | (2) | - | (1) |
| **Loss per year** | (2) | - | (9) |
| **Cash flows from discontinued operations** | | | |
| Net cash which derived from operating activities | - | - | 186 |
| Net cash which derived from investment activity | 25 | 22 | 131 |
| Net cash used for financing activity | - | - | (64) |
| **Net cash which derived from discontinued operations** | 25 | 22 | 253 |

## Note 9 - Investments in investee companies

### Material partnerships and consolidated companies that are held by the Company:

| | State of incorporation | Operating Segment | Rates of Ownership and Control of the Holding Company as of December 31, 2018 |
|---|---|---|---|
| | | | % |
| **Consolidated companies:** | | | |
| **Canit Hashalom Investments Ltd.** | Israel | Income-producing property | 100.00 |
| Gemel Tesua Investments Ltd. | Israel | Income-producing property | 100.00 |
| Otzma & Co. Investments Maccabim Ltd. | Israel | Income-producing property | 100.00 |
| Palace America Senior Housing Ltd. | Israel | Senior housing | 100.00 |
| Ahuzat Bayit Ra'anana – Retirement Home Ltd. | Israel | Senior housing | 100.00 |
| **Otzem Enterprise and Investments (1991) Ltd.** | Israel | Income-producing property | 100.00 |
| **AG Plaza at Enclave Inc.** | U.S. | Income-producing property | 100.00 |
| **Granite Hacarmel Investments Ltd. (*)** | Israel | Holdings | 100.00 |
| GES Global Environmental Solutions Ltd. | Israel | Treatment of water, wastewater and chemicals | 100.00 |
| Supergas Israel Gas Distribution Company Ltd. | Israel | Marketing of energy alternatives | 100.00 |
| **Azrieli E-Commerce Ltd.** | Israel | e-commerce | 100.00 |
| **Partnership – held by the Company, AG Galleria office buildings, LP** | U.S. | Income-producing property | 90.00 |
| **Assisted Living Modi'in Ltd.** | Israel | Senior housing | 100.00 |
| **AG Two Aspen, LP** | U.S. | Income-producing property | 100.00 |
| **AG 8 West Center LP** | U.S. | Income-producing property | 100.00 |
| **AG San Clemente 3700 LP** | U.S. | Income-producing property | 100.00 |

**Note 9 - Investments in investee companies (Cont.)**

(*) Restrictions applicable to Granite with respect to its subsidiaries:

**(1)** The ability of Granite's subsidiaries to distribute dividends to Granite is contingent upon their compliance with financial covenants which they undertook with respect to credit received from banks or upon obtaining the banks' consent or upon the provisions of the law.

**(2)** In tenders which companies in the Granite Group had won and/or in relation to agreements for the receipt of credit, restrictions were imposed on Granite with respect to the transfer of control and/or ownership, whereby the transfer of control and/or ownership shall be subject to the approval of the financing bodies or relevant governmental authorities, as the case may be.

**(3)** With respect to the sale of all of Granite Hacarmel's holdings in Sonol in 2016, see Note 8 on discontinued operations.

**Note 10 – Long term investments, loans and receivables**

**A. The composition:**

| | As of December 31 | |
|---|---|---|
| | **2018** | **2017** |
| | **NIS in millions** | **NIS in millions** |
| Loans provided (see B below) | 93 | 115 |
| Net of current maturities | (1) | (1) |
| | 92 | 114 |
| Authorities (see C below) | 36 | 73 |
| Assets in respect of employee benefits | 2 | 2 |
| Contract fulfillment costs | 14 | - |
| Receivables in respect of the averaging of income from rent | 144 | 110 |
| Restricted investments (see D below) | 19 | 19 |
| Other receivables | 36 | 28 |
| | 343 | 346 |

**B. Additional information:**

**(1)** For details with respect to a loan to the purchaser of Sonol, see Note 8 on discontinued operations.

**(2)** Unlinked loans in the sum of NIS 83 million were extended at an interest at the range of 2%-10% (in 2017 – approx. NIS 106 million).

In addition, index-linked loans in the sum of NIS 4 million were extended at an interest at the range of 0%-4% and NIS 6 million at an interest at the range of 4%-8% (in 2017 - an amount of NIS 2 million and NIS 7 million, respectively).

**C.** Including a sum of approx. NIS 29 million (2017 – approx. NIS 70 million) which is part of a betterment levy assessment that the Company paid under protest. Administrative appeals from the consulting appraiser's assessment have been submitted.

**D.** As collateral for the payment of bonds issued by a consolidated company of Supergas (see Note 19B(5)), the consolidated company provided for the benefit of the bond trustee an index-linked deposit in the amount of the highest quarterly payment (principal and interest) due according to the bond's payment schedule, until the repayment thereof.

## Note 11 - Financial assets

**The composition:**

| | As of December 31 | |
|---|---|---|
| | 2 0 1 8 | 2 0 1 7 |
| | NIS in millions | NIS in millions |
| Financial assets at fair value through profit and loss | 1,219 | 1,668 |
| Financial assets designated at fair value through profit and loss | 9 | 17 |
| | 1,228 | 1,685 |

**Financial assets at fair value through profit and loss:**

**A. Investment in Bank Leumi Le-Israel Ltd. ("Bank Leumi")**

On April 30, 2009 the Company acquired approx. 4.8% of the shares in Bank Leumi (approx. 71 million shares) for a consideration that was equivalent to NIS 742 million. In the course of the years 2017 and 2016 the Company sold approx. 16.7 million shares and approx. 5 million shares, respectively, in consideration for a sum of approx. NIS 203 million and approx. NIS 80 million, respectively, such that as of December 31, 2018, the Company held approx. 3.6% of Bank Leumi's shares. As a result of the sale of the shares in 2017 and 2016, financing income in the sum of approx. NIS 81 million and NIS 26 million, respectively, was recorded in these years.

As of the date of the Statement of Financial Position, the balance of the Company's investment in Bank Leumi's shares is approx. NIS 1,218 million (as of December 31, 2017 – NIS 1,132 million) according to the value of Bank Leumi's shares on TASE.

After the date of the Statement of Financial Position, the Company sold approx.7.5 million Bank Leumi shares in consideration for approx. NIS 180 million. Following the sale, the Company holds approx. 3.05% of the shares of Bank Leumi.

In 2018, the Company received a dividend in the sum of approx. NIS 49 million (in 2017 – approx. NIS 23 million) which was recorded under the Other Income item in the income statement. After the date of the Financial Statements, on March 6, 2019, it was decided at Bank Leumi to distribute a dividend that would be paid on April 3, 2019, with the Company's share in the dividend being approx. NIS 9 million.

**B. Investment in Leumi Card Ltd. ("Leumi Card")**

**(1)** In the Report Period and until February 25, 2019, the Company held 20% of the issued and paid-up capital of Leumi Card and 18% of the voting rights therein. In July 2018, the Company engaged, together with Bank Leumi Le-Israel Ltd. (the "**Bank**" and jointly the "**Sellers**"), in an agreement (the "**Agreement**") for the sale of all of the Sellers' holdings in Leumi Card Ltd. ("**Leumi Card**") to Warburg Pincus Financial Holdings (Israel) Ltd., a corporation controlled by the Warburg Pincus investment fund (the "**Buyer**").

As part of the terms and conditions of the Agreement, it was agreed that in consideration for the purchase of all of the Seller's shares in Leumi Card, the Buyer shall pay the Sellers a sum of NIS 2,500 million (apart from an adjustment to a dividend distribution and other adjustments according to the Agreement, if and insofar as Leumi Card distributes a dividend to its shareholders in the period up to the transaction closing date) in three installments at different rates, according to the dates fixed in the Agreement. The Company's share in the consideration before adjustments is NIS 500 million. The Agreement includes provisions regarding collateral, which the Buyer is obligated to provide to the Sellers as well as representations and indemnity provisions, specified in the Agreement. The Agreement included several conditions precedent, including receipt of the regulatory approvals required by law for the transaction.

**Note 11 - Financial assets (Cont.)**

**B. Investment in Leumi Card Ltd. ("Leumi Card") (Cont.)**

**(1) (Cont.)**

On February 25, 2019, the transaction was closed and the consideration therefor was received in accordance with the terms and conditions of the Agreement.

In 2018, Leumi Card distributed dividends in the sum of NIS 208 million (the Company's share is NIS 41.6 million), of which a sum of NIS 31.6 million was adjusted from the sale value (in 2017 approx. NIS 50 million was distributed – the Company's share was approx. NIS 10 million).

In February 2019, after the date of the financial statement, the Company received an additional dividend in the sum of NIS 80 million, which was adjusted from the sale value.

As of date of the Statement of Financial Position, the Company's investment balance in Leumi Card totaled at an amount of approx. NIS 450 million (as of December 31, 2017 – approx. NIS 536 million). In view of the agreement for the sale of the Company's holdings in Leumi Card, the investment in Leumi Card was classified to the assets held for sale item.

**(2)** In accordance with immediate reports released by Bank Leumi Le-Israel Ltd. ("**Bank Leumi**") on November 3, 2015 and December 23, 2015, Bank Leumi received notice from the companies Visa Inc. ("**Visa**") and Visa Europe Ltd. ("**Visa Europe**") regarding their engagement in an agreement, whereby Visa would acquire Visa Europe, and that the total consideration to be paid in the context of the transaction is estimated at up to approx. €21.2 billion, comprising payment in cash and in shares.

It was further stated in the reports of Bank Leumi that Bank Leumi is a member of Visa Europe. The Company, as the holder of 20% of the shares of Leumi Card, claimed that the consideration from the acquisition transaction of Visa Europe by Visa, originates from the business of Leumi Card vis-à-vis Visa Europe.

In April 2017, Bank Leumi and the Company agreed that Bank Leumi shall transfer to the Company, in respect of the Visa Europe transaction, a total amount of approx. NIS 32 million which were recognized as other income in the 2017 statements. Most of the amount was transferred to the Company in 2017.

**C.** On May 10, 2016, the Company engaged, directly and indirectly through companies controlled thereby, in sale agreements for the sale of all of the Company's holdings in the Pi Glilot lands and the shares of Pi Glilot Oil and Pipe Terminals Co. Ltd. (which is the owner of a leasehold with respect to land in the Pi Glilot site), to third parties, for a total consideration of approx. NIS 130 million.

During the Report Period, the transactions were closed and the consideration therefor was paid in accordance with the terms of the sale agreement. The closing of the transactions did not have a material effect on the Financial Statements.

## Note 12 - Long-term receivables in respect of franchise arrangements

**A. A franchise arrangement for the planning, construction and operation of a wastewater treatment plant:**

A consolidated company of GES has an agreement with local authorities for the planning, financing, building and maintenance of a wastewater treatment plant ("**WTP**"). Within the agreement, the Company undertook to build and operate the WTP for a term of 30 years, and in return the Company shall be entitled to an agreed payment per cubic meter, which is linked to the CPI. During 2012, an addendum to the agreement was signed, whereby the Company shall expand the existing WTP. In 2015, expansion of the WTP has been completed.

GES treats the expansion of the plant and its operation throughout its useful life, as a combined model which includes a financial asset - receivables in respect of a franchise arrangement and an intangible asset. GES recognizes revenue in accordance with IFRS 15.

**B. A franchise arrangement for the planning, construction and operation of a wastewater treatment facility for the recycling of water in production processes:**

On April 2, 2015, an agreement was signed between a consolidated company GES and a third party (the "**Customer**") for the rehabilitation, upgrade and operation of a facility for the recycling of wastewater.

In the agreement, after the completion of the construction, the Company undertook to operate the facility for a period of 10 years with an option for an extension of another 3 additional years.

The consolidated company accounts for the rehabilitation, upgrade of the facility and the operation thereof throughout its useful life as a financial asset - receivables in respect of a franchise arrangement. The consolidated company recognizes income throughout the construction period pursuant to IAS 11 and for the services it provides pursuant to IAS I8.

The upgrading of the facility has been completed and operation thereof has begun in April 2017.

**C. The collection dates of the balances for the receivables in respect of franchise arrangements after the date of the Financial Statements are as follows:**

| | As of December 31, 2018 | | | | | |
|---|---|---|---|---|---|---|
| | First year | Second year | Third year | Fourth year | Above five years | Total |
| | NIS in millions | | | | | |
| Receivables in respect of a franchise arrangement | 5 | 4 | 4 | 3 | 35 | 51 |

| | As of December 31, 2017 | | | | | |
|---|---|---|---|---|---|---|
| | First year | Second year | Third year | Fourth year | Above five years | Total |
| | NIS in millions | | | | | |
| Receivables in respect of a franchise arrangement | 5 | 5 | 4 | 4 | 37 | 55 |

## Note 13 - Investment property and investment property under construction

### A. Movements and composition:

| | As of December 31, 2018 | | | As of December 31, 2017 | | |
|---|---|---|---|---|---|---|
| | Land, buildings and leasable retail areas | Investment property under construction | Total | Land, buildings and leasable retail areas | Investment property under construction | Total |
| | NIS in millions | | | | | |
| **Balance as at the beginning of the year** | 23,319 | 1,887 | 25,206 | 20,003 | 3,720 | 23,723 |
| **Additions during the year:** | | | | | | |
| Investments | 1,280 | 584 | 1,864 | 391 | 732 | 1,123 |
| Adjustments to fair value | 140 | 78 | 218 | 47 | 453 | 500 |
| Net translation differences deriving from the translation of the financial statements of foreign operations | 169 | - | 169 | (206) | - | (206) |
| Entry into consolidation (*) | - | - | - | 124 | - | 124 |
| Transfer from investment property under construction, net | 101 | (101) | - | 3,000 | (3,000) | - |
| **Total additions** | 1,690 | 561 | 2,251 | 3,356 | (1,815) | 1,541 |
| **Write-offs during the year:** | | | | | | |
| Dispositions | 5 | - | 5 | - | - | - |
| Classification to fixed assets | - | - | - | - | 18 | 18 |
| Classification to assets held for sale (**) | - | - | - | 40 | - | 40 |
| **Total dispositions** | 5 | - | 5 | 40 | 18 | 58 |
| **Balance at the end of the year** | 25,004 | 2,448 | 27,452 | 23,319 | 1,887 | 25,206 |

(*) See Note 13D(2).
(**) See Note 11C.

### B. Additional information:

**(1)** Canit Hashalom is leasing the land on which the "Azrieli Center" was built from the Municipality of Tel Aviv-Jaffa under a capitalized lease for a period of 200 years. The lease period is until February 6, 2195. Mortgages apply to Canit Hashalom's leasehold in part of the lobby floor, the roof floor and floors 11-49 of the Round Tower, which constitutes part of Azrieli Center in Tel Aviv, in favor of an institutional body which provided the Company with a loan.

**(2)** From December 24, 2003, Canit Hashalom has been leasing the land on which the “Azrieli Modi'in" mall was built from the Israel Land Authority (ILA) under a capitalized lease for a period of 98 years in respect of residential units and for a period of 49 years in respects of units with other designations (the mall and offices) with an option for additional periods of 98 years and of 49 years, respectively. As of the date of the approval of the Financial Statements, the lease agreement has not yet been actually signed.

**(3)** The Company is leasing the land on which the "Azrieli Jerusalem (Malha)" mall was built from the ILA under a capitalized lease for a period of 49 years, ending on August 15, 2039, with an option for an additional period of 49 years.

**(4)** The Company is leasing the land on which the "Azrieli Ayalon" mall was built from the ILA under a capitalized lease for a period of 49 years, ending on August 1, 2031, with an option for an additional period of 49 years.

**Note 13 - Investment property and investment property under construction (Cont.)**

**B. Additional information: (Cont.)**

**(5)** The Company is leasing the land on which the Azrieli Or Yehuda Outlet Mall was built from the ILA under a capitalized lease for a period of 49 years, ending on March 24, 2040, with an option for an additional period of 49 years.

**(6)** The Company is leasing the land on which the Azrieli Givatayim Mall was built from the ILA under a capitalized lease for periods of 49 years, ending on September 5, 2053 and February 9, 2051, with an option for an additional 49-year term.

**(7)** The Company is leasing the land on which the Azrieli Haifa Mall was built from the ILA under a capitalized lease for periods of 49 years ending October 31, 2042 and March 2, 2035 with an option for an additional period of 49 years. The rights in the property are subject to pledges in favor of a bank that extended loans to the Company.

**(8)** The Company is leasing the land on which the industrial buildings in Caesarea Industrial Park were built from the Caesarea Edmond Benjamin de Rothschild Development Corporation Ltd. under a capitalized lease for a period of 49 years, ending on July 7, 2053 and March 12, 2049, with an option for an additional period of 49 years.

**(9)** The Group is leasing the land on which the Ramla Azrieli Mall was built from the ILA under a capitalized lease until January 14, 2050. As of the date of approval of the Financial Statements, the lease agreement has not yet been signed. The rights in the land are subject to pledges in favor of an institutional body which provided the Company with a loan.

**(10)** Canit Hashalom is leasing parts of the land on which the Azrieli Holon Center was built from the Municipality of Holon under a capitalized lease, in accordance with its share in the transaction for a period of 99 years, with an option for another 99 years for payment.

On the Group’s engagement with the Municipality of Holon through Canit Hashalom, see Note 29B(8).

**(11)** The Company is leasing the land on which the Sarona Tower was built and Sarona Mall is under construction from the ILA under a capitalized lease for a period of 49 years, ending on May 29, 2060 with an option for an additional period of 49 years from the end of the lease period.

**(12)** The Group is entitled to be registered as the owner of a sub-leasehold from the municipality in the framework of a set of agreements with a third party, in Palace Tel Aviv Senior Housing, until 2097.

**(13)** The Group is leasing the land on which Palace Modi’in Senior Housing was built from ILA under a capitalized lease for a period of 49 years, ending on January 25, 2063, with an option for an additional period of 49 years.

**(14)** The rights in the properties in the Azrieli Rishonim Center are subject to pledges in favor of an institutional body which provided the Company with a loan.

**(15)** The remaining income-producing properties are owned by the Group’s companies.

**(16)** In respect of additional charges and guarantees, see Note 30.

**Note 13 - Investment property and investment property under construction (Cont.)**

**B. Additional information: (Cont.)**

**(17)** The Group has several additional development projects in the retail centers and malls segment and in the leasable office and other space segment and in the senior housing segment:

- **Azrieli Town project** – in Tel Aviv on an area of approx. 10,000 sqm. The land on which the project is built is partially owned and partially leased in a capitalized lease from the ILA for 49 years, ending on May 8, 2061 with an option for an additional period of 49 years.

- **Expansion of Azrieli Center Tel Aviv** – in Tel Aviv, on an area of approx. 8,400 sqm, under ownership. In October 2017, the Company received approval from the District Committee for publication of a plan for validation for additional rights for commerce, offices, hospitality, residences and senior housing, such that the total building rights on the project land will amount to approx. 150 thousand sqm. As of the Report Date, the zoning plan has been published and validated.

- **Lodzia** – in Holon on an area of approx. 57,500 sqm, under ownership, including within it an additional plot of land that was originally purchased in an ILA tender and constituted part of the land of Holon HaManor.

- **HaManor Holon** – in Holon on an area of 6,200 sqm, under ownership.

- **A lot in Akko** – on an area of approx. 4,000 sqm, leased in a capitalized lease from the Municipality of Akko for a period ending on October 11, 2114.

- **Petah Tikva** – on September 17, 2017, the Company entered into an agreement, through an (indirect) wholly-owned subsidiary (the “**Purchaser**”), with unrelated third parties for the acquisition of land in Petah Tikva (the “**Land**") in consideration for NIS 91 million. On November 9, 2017 the transaction was closed and possession of the Land was handed over to the Group. The Land is on an area of about 19 thousand sqm located in the Eastern part of the Kiryat Aryeh industrial zone in Petah Tikva, close to an office project owned by the Purchaser. The Land includes rights for the construction of approx. 53,000 sqm. as well as parking basements. The Company intends to build an office project on the Land in accordance with the usages permitted under the zoning plan applicable to the Land. The Group is in the process of increasing the building rights in the project to 150,000 sqm.

- **Modi’in** – On January 11, 2018, a wholly-owned consolidated company won a tender held by the ILA for the purchase of capitalized leasehold rights for a term of 98 years ending on January 9, 2116, with an option for an additional 98-year term, in a lot located in Modi'in-Maccabim-Re’ut CBD, on an area of approx. 5,300 sqm, designated for the construction of 80 residential units, 50 hotel rooms, offices and commerce, in consideration for approx. NIS 101.5 million. The consolidated company is examining the possibility of taking action to increase the building rights in the lot.

- **Azrieli Town Building E (Mivnei Gazit)** – On April 22, 2018, the Company entered into an agreement with unrelated third parties (the “**Sellers**”) for the purchase of rights to land (some under ownership and some under capitalized leasehold from the ILA for a 49-year term ending on February 5, 2060) located on Menachem Begin Road, Tel Aviv, holding a 4-floor building over a commercial ground floor, in the total area of approx. 5,500 sqm and underground floors mostly leased for office purposes. The property includes unused building rights under the zoning plan that applies to the land, in the total scope of approx. 21,000 sqm above-ground, as well as the Sellers’ rights to lease underground areas in an adjacent plot, which are intended for the expansion of the building’s parking basements. In consideration for the purchase of rights to the land, the Company paid the Sellers NIS 260 million (exclusive of V.A.T.). The transaction was closed on May 14, 2018.

**Note 13 - Investment property and investment property under construction (Cont.)**

**B. Additional information: (Cont.)**

**(17) (Cont.)**

- **Palace Lehavim Senior Housing** – in Lehavim, on an area of 28,000 sqm, leased under a capitalized lease from the ILA for 49 years, ending on November 30, 2063, with an option for another period of 49 years.

- **Palace Rishon LeZion Senior Housing** – in Rishon LeZion on an area of approx. 3,400 sqm leased in a capitalized lease from the ILA for 49 years, ending on March 12, 2065 with an option for an additional period of 49 years.

**(18)** Some of the assets of consolidated companies are registered in their names in the Lands Registry. Another part has not yet been registered for technical reasons, the main reason for the non-registration deriving from the proceedings of the land arrangements and the reparcellation arrangements of the land have not yet been settled.

**(19)** With respect to techniques for the fair value estimation of the Group's investment property, see Note 34B(3). In addition, the fair value of the investment property is presented in the Company's books, with reconciliations for receivables in respect of the averaging of income from rent (see Note 10).

**(20) The amounts recognized in the income statement:**

| | As of the year ended December 31 | | |
|---|---|---|---|
| | **2018** | **2017** | **2016** |
| | **NIS in millions** | **NIS in millions** | **NIS in millions** |
| Rental, management and maintenance income | 2,063 | 1,868 | 1,745 |
| Direct operating expenses deriving from rent, management and maintenance | 543 | 484 | 445 |

**C.** With respect to an engagement in agreements for the sale of land in Pi Glilot in 2017 – see Note 11C.

**D. Income-producing property in the U.S.:**

**(1)** In August 2017, the city of Houston in the U.S. was hit by the tropical storm Harvey, that caused significant flooding, mainly in residential buildings in the city. a consolidated company holds parts of two office properties in Houston that incurred water damage during the storm. These assets are covered by insurance policies. The deductibles under such insurance policies amount to the total of approx. $10.6 million. The consolidated company's share in the deductible as of the date of the Statement of Financial Position is approx. $7.2 million (for details regarding income from indemnification from the insurance company, see Note 26).

**(2)** In December 2017, a consolidated company acquired the share of one of the partners at the rates of 33.33% and 25% in two office properties in Houston, Texas, known as One Riverway and Three Riverway, respectively, such that after the closing of the said acquisitions the Group holds 66.66% and 70% of such properties, respectively, in consideration for a capital injection in the sum of approx. $2.4 million and assumption of the said partner's share in loans in the sum of approx. $38.7 million.

**Note 13 - Investment property and investment property under construction (Cont.)**

**D. Income-producing property in the U.S.: (Cont.)**

**(3)** On July 12, 2018, the Company, through an (indirectly) wholly-owned American corporation, closed the acquisition of an office building in Austin, Texas, U.S. (the "**Property**"), in consideration for the sum of approx. U.S. $100.4 million. The Property is a 5-floor office building with a total area of approx. 23,214 sqm (approx. 249,870 sq. ft.) and an occupancy rate of approx. 100%. The Property also includes approx. 970 parking spaces, most of which are situated in a nearby 7-floor car park.

**E. Projected revenues due to signed lease contracts:**

Set forth below are the minimal lease payments due to be received due to lease contracts for the agreement periods (including revenues from rent, management fee and parking and excluding extension options):

| The revenue recognition period | Revenues from fixed components | |
|---|---|---|
| | 2018 | 2017 |
| | NIS in millions | NIS in millions |
| Up to one year | 1,860 | 1,677 |
| From one to four years | 3,714 | 3,488 |
| Over four years | 1,934 | 1,933 |
| | 7,508 | 7,098 |

## Note 14 - Fixed assets

### A. The movement and composition:

| | Land and buildings at cost | Machines and equipment | Furniture, equipment and computers | Vehicles | Installations and leasehold improve-ments | Total |
|---|---|---|---|---|---|---|
| | NIS in millions | | | | | |
| **Cost:** | | | | | | |
| **Balance as of January 1, 2017** | 178 | 671 | 111 | 50 | 13 | 1,023 |
| Additions | 28 | 35 | 6 | 12 | 2 | 83 |
| Write-offs | - | (2) | - | (3) | - | (5) |
| Classified from investment property | 18 | - | - | - | - | 18 |
| Effect of changes in exchange rate | (3) | (2) | - | - | - | (5) |
| **Balance as of December 31, 2017** | 221 | 702 | 117 | 59 | 15 | 1,114 |
| Additions | 25 | 31 | 6 | 4 | 1 | 67 |
| Write-offs | - | - | (1) | (3) | - | (4) |
| Effect of changes in exchange rate | 2 | 2 | - | 2 | - | 6 |
| **Balance as of December 31, 2018** | 248 | 735 | 122 | 62 | 16 | 1,183 |
| **Accumulated depreciation and loss from impairment:** | | | | | | |
| **Balance as of January 1, 2017** | 32 | 443 | 75 | 17 | 11 | 578 |
| Depreciation for the year | 4 | 25 | 4 | 5 | 1 | 39 |
| Write-offs | - | (1) | - | (2) | - | (3) |
| **Balance as of December 31, 2017** | 36 | 467 | 79 | 20 | 12 | 614 |
| Depreciation for the year | 5 | 25 | 5 | 6 | 1 | 42 |
| Write-offs | - | - | (1) | (2) | - | (3) |
| **Balance as of December 31, 2018** | 41 | 492 | 83 | 24 | 13 | 653 |
| **Depreciated Cost:** | | | | | | |
| **As of December 31, 2018** | 207 | 243 | 39 | 38 | 3 | 530 |
| **As of December 31, 2017** | 185 | 235 | 38 | 39 | 3 | 500 |

### B. On charges - see Note 30.

### C. Details in respect of interests in land used by the Group as fixed assets

**(1)** Consolidated companies in the Granite Group have buildings on lands held under capitalized lease from the ILA for various periods until 2059. The depreciated cost of the buildings on leased lands and the leased lands, as of December 31, 2018 is NIS 55 million (December 31, 2017 - NIS 55 million).

**(2)** With respect to the land rights of the senior homes' LTC units, see Note 13B.

## Note 15 - Intangible assets

### A. The movement and composition:

| | Goodwill | Customer relations | Rights to supply and distribution rights to oil distillates and others | Franchise arrangements | Software | Others (*) | Total |
|---|---|---|---|---|---|---|---|
| | | | | NIS in millions | | | |
| **Cost:** | | | | | | | |
| **Balance as of January 1, 2017** | 170 | 115 | 125 | 20 | 70 | 31 | 531 |
| Additions | - | - | - | - | 2 | - | 2 |
| **Balance as of December 31, 2017** | 170 | 115 | 125 | 20 | 72 | 31 | 533 |
| Additions | - | - | 5 | 6 | 1 | 1 | 13 |
| Effect of changes in exchange rates | - | - | - | 1 | - | - | 1 |
| Write-offs | - | - | - | - | - | (1) | (1) |
| **Balance as of December 31, 2018** | 170 | 115 | 130 | 27 | 73 | 31 | 546 |

(*) The 'Others' item includes primarily amounts in respect of a brand, trademarks and licenses and rights for the supply of natural gas.

## Note 15 - Intangible assets (Cont.)

### A. The movement and composition (Cont.):

| | Goodwill | Customer relations | Rights to supply and distribution rights to oil distillates and others | Franchise arrangements | Software | Others | Total |
|---|---|---|---|---|---|---|---|
| | | | | NIS in millions | | | |
| **Amortizations and losses from impairment:** | | | | | | | |
| **Balance as of January 1, 2017** | 4 | 86 | 62 | 3 | 31 | 12 | 198 |
| Amortization for the year | - | 4 | 5 | 1 | 10 | 5 | 25 |
| **Balance as of December 31, 2017** | 4 | 90 | 67 | 4 | 41 | 17 | 223 |
| Amortization for the year | - | 4 | 8 | 3 | 10 | 3 | 28 |
| Write-offs | - | - | - | - | - | (1) | (1) |
| **Balance as of December 31, 2018** | 4 | 94 | 75 | 7 | 51 | 19 | 250 |
| **Book value:** | | | | | | | |
| As of December 31, 2018 | 166 | 21 | 55 | 20 | 22 | 12 | 296 |
| As of December 31, 2017 | 166 | 25 | 58 | 16 | 31 | 14 | 310 |

| **Original Amount of Goodwill:** | NIS in Millions |
|---|---|
| As of December 31, 2016 | 178 |
| As of December 31, 2017 | 178 |
| As of December 31, 2018 | 178 |

**Note 15 - Intangible assets (Cont.)**

**B. Allocation of goodwill to cash generating units:**

**The goodwill has been allocated to cash generating units for the purposes of the testing for impairment, as follows:**

| | As of December 31 | | |
|---|---|---|---|
| | 2018 | 2017 | 2016 |
| | NIS in millions | NIS in millions | NIS in millions |
| Activity B – Gas (1) | 63 | 63 | 63 |
| Activity C – Senior Housing | 77 | 77 | 77 |
| Activity D – E-commerce (2) | 26 | 26 | 26 |
| | 166 | 166 | 166 |

**Key assumptions used to calculate a recoverable amount:**

**(1)** The testing for impairment of goodwill was determined based on the discounting of the future cash flows to be generated from the continuous use of the units, and based on the following assumptions:

**(a)** The cash flow is estimated based primarily on the actual results of activity and on a business plan for the coming five years.

**(b)** The main projected annual growth rate that is included in the cash flow forecast in the representative year is 2.2% (last year – 2.3%), in accordance with management's evaluation. This growth rate is based on the long-term growth rate of the GDP, the rate of population growth in Israel, business trends in operations in each sector and on the expected increase in competition for the various products.

**(c)** For the purpose of estimation of the cost of capital for the activity, an estimate was made of the pre-tax weighted average cost of capital (WACC), while using the CAPM model for the calculation of the cost of capital and additional assumptions in respect of the price of debt and its appropriate debt structure. In determination of the recoverable amount of the units, a cap rate of 13.02% (2017 – 13.80%) was used. The estimate of the cap rate was made in reliance, *inter alia*, on the cost of capital for each activity (including the taking into consideration of the risk free interest rate, the market premium and the beta), the price of debt and comparison to similar public companies and other competing companies, as the case may be.

**(2)** The testing for impairment of goodwill was determined based on the discounting of the future cash flows to be generated from the continuous use of the unit, and based on the following assumptions:

**(a)** The cash flow is estimated based on forecasts for the next seven years, which take into account that the Company is in the process of penetrating the Israeli e-commerce market.

**(b)** The main projected annual growth rate that is included in the cash flow forecast in the representative year is 4% (2017 – 8%), which represents the projected growth of the e-commerce market in Israel.

**(c)** For the purpose of estimation of the cost of capital for the activity, an estimate was made of the pre-tax weighted average cost of capital (WACC), while using the CAPM model for the calculation of the cost of capital and additional assumptions. In determination of the recoverable amount of the units, a cap rate of 15.25% was used (2017 – 15.96%).

**Note 15 - Intangible assets (Cont.)**

**B. Allocation of goodwill to cash generating units (Cont.):**

**Key assumptions used to calculate a recoverable amount: (Cont.)**

The evaluations and the assumptions were determined in accordance with the estimations of the managements in the Group in respect of future trends in the sector, and they are based on both external and internal sources (historical data) and in accordance with economic evaluations by independent appraisers.

**Note 16 - Trade payables**

**The composition:**

| | As of December 31 | |
|---|---|---|
| | 2018 | 2017 |
| | NIS in millions | NIS in millions |
| Open debts | 241 | 211 |
| Checks payable | 101 | 85 |
| | 342 | 296 |

**Note 17 - Other payables**

**The composition:**

| | As of December 31 | |
|---|---|---|
| | 2018 | 2017 |
| | NIS in millions | NIS in millions |
| Advance payments from customers and income in advance | 38 | 43 |
| Liabilities for the completion of work in progress | 4 | 8 |
| Liabilities to employees and other liabilities in respect of salaries and wages | 39 | 37 |
| Interest and expenses payable | 105 | 70 |
| Institutions | 29 | 27 |
| Advance payment on account of sale of investment property | - | 8 |
| Others | 10 | 8 |
| | 225 | 201 |

For further information regarding payables that constitute related and interested parties, see Note 35C.

**Note 18 - Deposits from customers**

**A.** Supergas collects from its customers a deposit for ensuring the recovery of the equipment provided to them at the time of the engagement therewith, which it is required to return upon the end of the engagement and the recovery of the equipment, in accordance with the Products and Services Price Control Order (Determination of the Level of Control and Maximum Deposit Prices for Gas Equipment) 5776-2015.

**B. Liability due to senior housing deposits and liabilities due to apartment keeping deposits**

The Group has liabilities due to Shekel deposits received from residents with whom contracts were signed in senior housing projects, which are operated by the Group. The liabilities due to the Shekel deposits are linked to the CPI and are presented after erosion pursuant to the agreements signed by the Group's companies with residents.

**Note 18 - Deposits from customers (Cont.)**

According to agreements with some of the residents, a certain percentage of the balance of the deposits is used as an advance payment for the residents' rights of usage of the property and is not repaid to the residents. The "income received in advance" component is included as part of the liability due to the deposits and is carried to the income statement as income throughout the term of the agreement.

Furthermore, there are liabilities due to apartment keeping deposits.

**Note 19 - Loans from financial corporations**

**A. Current liabilities:**

| | As of December 31 | |
|---|---|---|
| | 2018 | 2017 |
| | NIS in millions | NIS in millions |
| **Credit from banks** | | |
| Overdrafts | 1 | - |
| Short-term loans | 46 | 47 |
| | 47 | 47 |
| **Credit from other credit providers** | | |
| Commercial paper (*) | 436 | 582 |
| Short-term loans | 1 | 1 |
| | 437 | 583 |
| **Current maturities of long-term liabilities** | | |
| Current maturities of loans from banks | 119 | 90 |
| Current maturities of loans from others | 283 | 362 |
| Current maturities of bonds | 679 | 429 |
| | 1,081 | 881 |
| **Total current liabilities** | 1,565 | 1,511 |

(*) On June 23, 2014, the Company issued a (rated) series of commercial paper for investors listed in the First Schedule to the Securities Law, 5728-1968, with a total par value of NIS 480 million. The commercial paper principal bears variable NIS interest comprising Prime interest less 1.2%, payable after the earlier of twenty 90-day terms or at maturity or at an exit point. The commercial paper will not be listed on TASE.

The commercial paper received an "ilA-1+" rating from Ma'alot.

Since then the Company has repaid a par value of approx. NIS 185 million out of this series, and the balance of the rated commercial paper series as of December 31, 2018 is in the par value of approx. NIS 295 million.

In March 2015, the Company issued a new unrated series of commercial paper with a total par value of NIS 116 million. Since then, this series has been expanded on the one hand, and there have been several repayments on the other hand, such that, as of December 31, 2018, the balance of the par value of the unrated series of commercial paper is approx. NIS 140 million. After the date of the Statement of Financial Position, the Company expanded this series by a par value of NIS 42 million. The principal of the commercial paper bears variable shekel interest comprised of the Prime interest rate less 1.2%, and shall be paid at the end of twenty 90-day terms or at maturity or at an exit point, whichever is earlier.

**Note 19 - Loans from financial corporations (Cont.)**

**B. Non-current liabilities:**

| | As of December 31 | |
|---|---|---|
| | **2018** | **2017** |
| | **NIS in Millions** | **NIS in Millions** |
| **Bonds** | | |
| Bonds (1), (2), (3), (4), (5) | 6,844 | 5,864 |
| **Loans from banks** | 217 | 244 |
| **Other long-term liabilities** | | |
| Long-term loans from others | 2,411 | 2,512 |
| | 9,472 | 8,620 |
| Net of current maturities | (1,081) | (881) |
| **Total non-current liabilities** | 8,391 | 7,739 |
| **Presented under the following items:** | | |
| Loans from banks and other credit providers | 2,226 | 2,304 |
| Bonds | 6,165 | 5,435 |
| | 8,391 | 7,739 |

**(1)** In February 2015, the Company made a public offering of approx. NIS 623.3 million par value of registered Series B Bonds, based on the Company's shelf prospectus. The bonds are linked (principal and interest) to the CPI and bear interest at a fixed rate of 0.65% per year.

The principal payments will be paid in 10 equal annual installments on April 1 of each one of the years 2016 to 2025 (each installment will be 10% of the principal's par value). The interest will be paid in semiannual installments from October 1, 2015 and on April 1 and October 1 of each one of the years 2016 to 2025. The bonds were issued without a discount.

The effective interest rate in respect of the bonds is 0.78% per annum.

On January 20, 2015, Ma'alot rated the Series B Bonds as ilAA+ (stable outlook).

The bonds are not secured by any collateral.

At the time of the offering, the Company undertook to meet financial covenants and undertakings, the main ones being:

**(a)** So long as the Series B Bonds are not fully paid-up, the Company shall neither encumber nor pledge by way of a floating charge all of the Company's existing or future assets and rights, except under certain conditions set forth in the Indenture.

**(b)** Maintaining minimal equity (equity attributable to the Company's shareholders, excluding minority rights) of at least NIS 5 billion for two or more consecutive calendar quarters, according to its last consolidated financial statements.

**Note 19 - Loans from financial corporations (Cont.)**

**B. Non-current liabilities: (Cont.)**

**(1) (Cont.)**

**(b) (Cont.)**

The net financial debt to net assets ratio, according to the definitions in the Indenture, exceeded 60% for two or more consecutive calendar quarters.

The Indenture determines that in lieu of the said financial covenants, the Company may, at its sole discretion, pledge (either itself or through an investee company) in favor of the trustee for the Series B bondholders, by way of a fixed charge, Permitted Assets as defined in the Indenture (i.e., insofar as the Company pledges Permitted Assets as aforesaid, and the pledges are in force and effect, the Company shall not be bound by the said financial covenants).

**(c)** The Company shall not perform a Distribution (as defined in the Companies Law) to its shareholders, if: (1) the Company's equity (equity attributable to the Company's shareholders, excluding minority rights) according to its last published consolidated financial statements, net of the amount of the Distribution, is less than NIS 6 billion; (2) the Company's net financial debt to net assets ratio (as defined in the Indenture), net of the amount of the Distribution, exceeds 50%; (3) there are grounds for acceleration according to the definitions in the Indenture of the Series B Bonds on the date of the decision to perform the Distribution or as a result thereof.

As of the balance sheet date, the Company meets the financial covenants, with the Company's equity as of the balance sheet date being approx. NIS 17.1 billion and the net financial debt to net assets ratio is approx. 29%.

It was further determined that in the event that the rating of the Company's Series B Bonds falls below Ma'alot's ilAA rating, or a corresponding rating determined by another company that rates the bonds, the rate of the annual interest borne by the unpaid balance of the bond principal shall rise, in which case, the annual interest rate that shall be added to the annual interest in respect of the bonds will range between 0.25% and 1%, according to the bonds' rating.

In addition, the Series B Bonds shall be accelerated upon fulfillment of certain conditions, including: delisting or dissolution of the Company, receivership, delinquency in payments under the bonds, attachments on all or most of the Company's assets, changes in control, a fundamental breach of the terms and conditions of the bonds or the Indenture, non-compliance with the above financial covenants, performance of a distribution contrary to the above restriction on the performance of a distribution, suspension of trading of the bonds (except on grounds of ambiguity), a demand for acceleration by financial creditors above NIS 200 million or another bond series of the Company, discontinuation of rating of the bonds due to circumstances within the Company's control, a bond rating lower than BBB-, or the sale of most of the Company's assets.

In June 2015, the Company made another public offering of approx. NIS 600.3 million par value by way of expansion of the Series B Bond series, at a price of 100.24 Agorot per NIS 1 par value (discounting at a rate of 0.44% relative to their adjusted value) based on a shelf prospectus of the Company.

In March 2017, the Company made another public offering of NIS 228.8 million par value of Series B Bonds, at a price of 97.45 Agorot per NIS 1 par value (discounting at a rate of approx. 2.55% relative to their adjusted value), by way of expansion of the bond series, based on a shelf prospectus of the Company. The gross issue proceeds amounted to NIS 223 million, and the net proceeds net of the issue expenses amounted to approx. NIS 221.2 million.

**Note 19 - Loans from financial corporations (Cont.)**

**B. Non-current liabilities: (Cont.)**

**(1) (Cont.)**

The balance of the Series B Bonds, principal and linkage differentials (net of issue expenses and discounting) as of December 31, 2018 is NIS 1,047 million (as of December 31, 2017 – NIS 1,193 million).

**(2)** In September 2015, the Company made a public offering of approx. NIS 1,005.1 million par value registered Series C Bonds based on a shelf prospectus of the Company. The bonds are linked (principal and interest) to the CPI and bear fixed interest at a rate of 1.64% per annum.

The principal payments will be made in 10 equal annual installments on July 1 of each one of the years 2018-2027 (each installment will be 10% of the principal's par value). The interest will be paid in semi-annual installments from July 1, 2016 and on January 1 and July 1 of each one of the years 2017-2027. The bonds were issued without any discount.

The effective interest rate in respect of the bonds is 1.78% per annum.

On September 3, 2015, Ma'alot rated the Series C Bonds as ilAA+.

The bonds are not secured by any collateral.

At the time of the offering, the Company undertook to meet financial covenants and undertakings, similar to the financial covenants to which it committed in respect of the Series B Bonds (for a description of the terms and conditions and the meeting of the financial covenants, see Section 1 above).

It was further determined that in the event that the rating of the Company's Series C Bonds falls below Ma'alot's ilAA rating, or a corresponding rating determined by another company that rates the bonds, the annual interest rate borne by the unpaid balance of the bond principal shall rise, in which case, the annual interest rate that shall be added to the annual interest in respect of the bonds will range between 0.25% and 1%, according to the bonds' rating.

In addition, the Series C Bonds shall be accelerated upon fulfillment of certain conditions, similar to the terms that were determined in respect of the Series B Bonds (for a description of the terms and conditions, see Section 1 above).

In March 2017, the Company made another public offering of NIS 179 million par value of Series C bonds, at a price of 101.4 Agorot per NIS 1 par value (premium at a rate of approx. 1% relative to their adjusted value), by way of expansion of the bond series, based on a shelf prospectus of the Company. The gross issue proceeds amounted to NIS 181.5 million, and the net proceeds net of the issue expenses amounted to approx. NIS 180.8 million.

The balance of the Series C Bonds, principal and linkage differentials (net of issue expenses) as of December 31, 2018 is NIS 1,063 million (as of December 31, 2017 – NIS 1,178 million).

**(3)** In July 2016, the Company issued approx. NIS 2,194.1 million par value registered Series D bonds to the public, on the basis of a shelf prospectus of the Company. The bonds are linked (principal and interest) to the CPI and bear fixed interest at the rate of 1.34% per annum.

The principal payments shall be made in 25 equal semi-annual installments on January 5 and July 5 of each of the years 2018 to 2030 (each payment being at the rate of 4% of the par value of the principal from July 5, 2018). The interest will be paid in semi-annual payments from January 5, 2017 of each of the years 2017 to 2030. The bonds were issued without a discount.

**Note 19 - Loans from financial corporations (Cont.)**

**B. Non-current liabilities: (Cont.)**

**(3) (Cont.)**

The issue proceeds amounted to approx. NIS 2,194 million, and net of the issue expenses, the net proceeds amounted to approx. NIS 2,177 million. The effective interest rate on the bonds is 1.45% per annum.

On July 5, 2016, Midroog assigned the Series D bonds a stable Aa1 rating, and on July 20, 2016, Midroog ratified this rating.

The bonds are not secured by any collateral.

At the time of the offering, the Company undertook to meet financial covenants and undertakings similar to the financial covenants undertakings to which it committed in respect of the Series B and C Bonds (for a description of the terms and conditions – see Section 1 above).

It was further determined that in the event that the rating of the Company's Series D Bonds falls below Midroog's Aa2 rating, or a corresponding rating that is determined by another company that rates the bonds, the annual interest rate borne by the unpaid balance of the bond principal shall rise, in which case, the annual interest rate that shall be added to the annual interest in respect of the bonds will range between 0.25% and 1%, according to the bonds' rating.

In addition, the Series D Bonds shall be accelerated upon fulfillment of certain conditions, similar to the conditions that were determined in respect of the Series B and C Bonds (for a description of the terms and conditions and the meeting of the financial covenants – see Section 1 above).

In March 2017, the Company made another public offering of NIS 983.6 million par value of Series D Bonds, at a price of 97.6 Agorot per NIS 1 par value (discounting at a rate of approx. 2.7% relative to their adjusted value), by way of expansion of the bond series, based on a shelf prospectus of the Company. The gross issue proceeds amounted to NIS 960 million, and the net proceeds net of the issue expenses amounted to approx. NIS 955.3 million.

In February 2018, the Company made another public offering of NIS 1,367 million par value of the Company's Series D Bonds by way of expansion of the bonds series, at a price of 103.1 Agorot per NIS 1 par value (premium at a rate of approx. 2.5% with respect to their adjusted value), based on a shelf prospectus of the Company. The gross issue proceeds amounted to approx. NIS 1,409 million, and the net proceeds net of the issue expenses amounted to approx. NIS 1,400 million.

The balance of the Series D Bonds, principal and linkage differentials (net of issue expenses) as of December 31, 2018 is NIS 4,411 million (as of December 31, 2017 - NIS 3,142 million).

**(4)** After the date of the Statement of Financial Position, in January 2019, the Company issued to the public registered Series E Bonds in the nominal value of approx. NIS 1,216 million, based on the Company's shelf prospectus. The bonds are linked (principal and interest) to the Consumer Price Index and bear a fixed interest rate of 1.77% per annum.

The Series E Bonds will be payable (principal) in 7 annual, consecutive but not equal, payments, paid on June 30 of each of the years 2022 to 2028 as specified below:

The first and second payments will be paid on June 30 of the years 2022 and 2023 and will each be at the rate of 7.5% of the nominal value of the principal. The third and fourth payments will be paid on June 30 of the years 2024 and 2025 and will each be at the rate of 5% of the nominal value of the principal. The fifth, sixth and seventh payments (the seventh being the last) will be paid on June 30 of the years 2026, 2027 and 2028 and will each be at the rate of 25% of the nominal value of the principal.

**Note 19 - Loans from financial corporations (Cont.)**

**B. Non-current liabilities: (Cont.)**

**(4) (Cont.)**

Interest will be paid in semiannual payments as of June 30, 2019 in each of the years 2019 to 2028. The bonds were issued without discount.

The proceeds of the issuance totaled approx. NIS 1,216 million, and after deduction of the issuance expenses, the net proceeds totaled approx. NIS 1,207 million. The effective interest rate for the bonds is 1.86% per annum.

After the date of the Statement of Financial Position, in January 2019, the Company issued to the public registered Series F Bonds in the nominal value of approx. NIS 263.4 million, based on the Company's shelf prospectus. The bonds are linked (principal and interest) to the Consumer Price Index and bear a fixed interest rate of 2.48% per annum.

The Series F Bonds will be payable (principal) in 8 annual, consecutive but not equal, payments, paid on December 31 of each of the years 2025 to 2032 as specified below:

The first payment will be paid on December 31, 2025 and will be at the rate of 2.5% of the nominal value of the principal. The second payment will be paid on December 31, 2026 and will be at the rate of 5% of the nominal value of the principal. The third payment will be paid on December 31, 2027 and will be at the rate of 7.5% of the nominal value of the principal. The fourth payment will be paid on December 31, 2028 and will be at the rate of 10% of the nominal value of the principal. The fifth payment will be paid on December 31, 2029 and will be at the rate of 15% of the nominal value of the principal. The sixth, seventh and eighth payments (the eighth being the last) will be paid on December 31 of the years 2030, 2031 and 2032 and will each be at the rate of 20% of the nominal value of the principal.

Interest will be paid in semiannual payments from June 30, 2019 to December 31, 2032. The bonds were issued without discount.

The proceeds of the issuance totaled approx. NIS 263 million, and after deduction of the issuance expenses, the net proceeds totaled approx. NIS 260 million. The effective interest rate for the bonds is 2.57% per annum.

On January 7, 2019 and January 20, 2019, Midroog approved an Aa1 rating for the issuance of new series (Series E and Series F) (collectively: the "**Bonds**").

The Bonds are not secured by any collateral and will be of equal rank in respect of the sums due therefor, *pari passu*, *inter se*, without any preference right or priority of one over the other.

At the time of the issuance, the Company undertook to comply with financial covenants similar to the financial covenants undertaken thereby in respect of the Series B, C and D Bonds (for a description of the conditions – see Section 1 above), with the exception of the following:

In the event that a change occurs in the accounting standards applicable to the Company as compared with the accounting standards applicable to the Company on the date of issuance of the Series E Bonds and Series F Bonds for the first time, and such change has a material effect (as defined in the indenture) on the result of computation of any of the financial covenants (defined in the indenture), the Company shall examine such covenant according to a proforma income statement and balance sheet according to the standards on the date of the issuance.

**Note 19 - Loans from financial corporations (Cont.)**

**B. Non-current liabilities: (Cont.)**

**(4) (Cont.)**

It is further determined that if the rating of the Company's Series E Bonds and Series F Bonds drops below Midroog's Aa2 rating or an equivalent rating determined by another agency that shall rate the bonds, the annual interest rate to be borne by the outstanding principal of the bonds shall, in such case, increase by 0.5% up to 1%, insofar as the rating drops three tiers or more below such Aa2 rating.

Furthermore, the Series E Bonds and Series F Bonds shall be accelerated upon the fulfillment of certain conditions which are substantially similar to the conditions determined in relation to the Series B, C and D Bonds (for a description of the conditions and compliance with the financial covenants – see Section 1 above).

**(5)** In July 2007, a consolidated company of Supergas which was established for the purpose of the issuance, and to which, primarily, the domestic gas operations were transferred, executed an issue of bonds to institutional investors through a private placement, with a total par value of NIS 600 million. The bonds, which are rated with a rating of Aa1 by Midroog Ltd., are for a period of 18 years, and are repaid in quarterly installments of the principal from 2010. The bonds are linked to the CPI (principal and interest) and bear interest at a rate of 4.9% a year, which is paid once every calendar quarter. The balance of the bonds is presented net of issue expenses. The effective rate of interest for the bonds is 5.26% a year.

In addition, in accordance with the terms and conditions of the bonds, all of the income received from Supergas household customers are deposited into a special account, the signatory rights in which are given to the Company and the trustee for the bonds. After the making of the quarterly payment to the bondholders, and provided that the debt coverage ratio is at least 126.5%, the surplus income is transferred to the Company.

In June 2014, the consolidated company of Supergas completed a process to modify the bonds, which includes prepayment of certain principal payments (which constitute approx. 11.5% of the bond balance), which, according to the original terms of the issuance, were due to be paid over the coming five years, and in fixed quarterly principal payments such that they will be uniform and equal. Accordingly, the consolidated company of Supergas paid 51,829,380 par value in total of approx. NIS 75 million, which includes the sum of approx. NIS 12.3 million that was paid due to the prepayment. Such change was treated as an immaterial change of conditions, and the effective interest rate of the bonds was accordingly updated. As of January 1, 2018, concurrently with the adoption of IFRS 9 (see Note 2N) with respect to an immaterial change of liability conditions, the difference between the discounted future cash flows at the original interest rate and the book value of the liability (immediately prior to the change of conditions), was carried to profit and loss. Accordingly, a net balance of NIS 6,164 thousand was attributed to retained earnings as of the beginning of 2018.

In addition, it was determined that in the event that Canit Hashalom ceases to be a controlling shareholder of the Company, then Granite shall make an offer to the bondholders to purchase the bonds at a scope of no less than 45 million par value.

The bonds are secured by a first-ranking floating charge, in an unlimited amount, on all of the assets of the consolidated company of Supergas, in addition, Supergas charged by a first ranking fixed charge in an unlimited amount all of the shares of the consolidated company owned and held thereby, including the rights deriving from such shares.

In accordance with the terms and conditions of the bonds, the consolidated company of Supergas is required to meet financial covenants. Any deviation from the financial covenants will allow the bondholders to demand acceleration of the payment or prepayment, as described below.

**Note 19 - Loans from financial corporations (Cont.)**

**B. Non-current liabilities: (Cont.)**

**(5) (Cont.)**

**Acceleration:**

**(a)** If the ratio between the average quarterly free cash flows from the domestic gas operations (the cash flow of the receipts from the domestic operations net of actual purchases of gas and expenses in respect of the services agreement in respect of the domestic gas operations), for the past year and the quarterly installment (principal and interest) which are expected to be paid to the bondholders at the time of the next expected payment (the "**Debt Coverage Ratio**") falls below 111%.

**(b)** If the rate of the margin on the commercial gas operations in containers falls below 12% (as of the date of the Financial Statements, the rate of the margin is approx. 59%).

**Acceleration and realization of collateral:**

**1.** If the Debt Coverage Ratio falls below 103%.
**2.** In the event of insolvency.
**3.** The non-payment of a payment of principal or interest.
**4.** A decision for dissolution or receivership of Supergas' consolidated company.
**5.** The imposition of an attachment or execution of the entire or material assets of Supergas' consolidated company.
**6.** A fundamental breach of the terms of the bonds.
**7.** In the event that Supergas' consolidated company loses the gas license.
**8.** In the event of a change in control such that Granite ceases, under certain conditions, to control Supergas.
**9.** The lowering of the rating of the bonds rating below Baa1 or if the rating is not monitored.

In addition, there are grounds for the replacement of Supergas as a provider of services in the transaction, the main ones being: if the Debt Coverage Ratio falls below 106%; events in which Supergas becomes insolvent or if it loses its gas supplier license.

As of the date of the Financial Statements, Supergas's consolidated company meets the covenants while the Debt Coverage Ratio as of the Report Date is 345%.

The balance of the bonds, net of issue expenses as of December 31, 2018 is NIS 323 million (as of December 31, 2017 – NIS 351 million).

**(6)** On May 21, 2014, the Company entered into a loan agreement with several companies in an institutional body group affiliated neither with the Company nor with its controlling shareholders, to receive a loan of NIS 300 million, linked to the CPI, bearing annual interest at the rate of 0.74%. The loan (principal and interest) will be repaid in 36 equal quarterly installments linked to the rate of increase in the Index from the end of three months from the date of provision of the loan. To secure repayment of the loan, a consolidated company has pledged, in favor of the lender, its rights in the land on which the Azrieli Ramla Mall is being built, including its rights to receive rent from tenants in the Mall, and the Company's rights by virtue of the insurance policy in connection with the Mall will also be pledged. The lender will be entitled to accelerate the loan on accepted grounds that are set forth in the loan agreement, including, *inter alia*, upon the occurrence of a change of control, the acceleration of a debt of the Company to other financial institutions, or the imposition of an attachment in the amounts and under the conditions as are defined in the loan agreement, and also if after the population of the Mall and the opening thereof to the public, the LTV is higher than the ratio set forth in the loan agreement and no other or supplementary collateral was provided.

**Note 19 - Loans from banks and other credit providers (Cont.)**

**B. Non-current liabilities: (Cont.)**

**(6) (Cont.)**

It was further determined that if the Company grants a floating charge to another entity in the future, it shall grant the lender, on the same date, a floating charge of identical ranking and scope (*pari passu*).

As of December 31, 2018, the Company meets the financial covenants, with the LTV ratio required according to the agreement on this date being 45% and being 31% in practice.

**(7)** On May 24, 2016, a loan was provided to the Company in the sum of NIS 550 million from an institutional body affiliated neither with the Company nor with its controlling shareholders, linked to the CPI, at annual interest at the rate of 1.5%.The repayment of the loan's principal shall commence from the second anniversary of the date of provision of the loan and shall be made in 40 equal quarterly installments (the last principal payment shall be made 12 years after the date of provision of the loan). The interest on the loan shall be paid on a quarterly basis, until the final repayment date. The Company is entitled to prepay the loan (in whole or in part) against a prepayment fee according to a mechanism defined in the agreement.

To secure repayment of the loan, Canit Hashalom, a subsidiary wholly owned by the Company, pledged in favor of the lender, by way of a first-ranking fixed pledge unlimited in amount, the Azrieli Rishonim Center in Rishon LeZion, including its rights to receive rent from the property's tenants and its rights under the insurance policies in connection with the property.

In the context of the loan agreement, the Company undertook to meet the financial covenants that were set forth in the indentures of the Company's Series B and C bonds (the "**Bonds**"), i.e. a net debt to assets ratio that shall not exceed 60% and equity of no less than NIS 5 billion (the "**Financial Covenants**"), and it further undertook to maintain an LTV ratio that shall not exceed 80%, commencing from April 1, 2018. In addition, the agreement includes limitations on the distribution of a dividend that correspond with the undertaking set forth in the Bonds' indentures (i.e. that no distributions shall be made if, as a consequence thereof, the equity shall be less than NIS 6 billion and the debt to assets ratio shall exceed 50%). In addition, the Company undertook not to create a floating charge on all or part of the Company's assets, to any entity, unless it shall create in favor of the lender, on the same date, a floating charge of identical ranking and scope (*pari passu*) (such an undertaking also exists in the Bonds' indentures). The causes for acceleration are as customary in agreements of this type and in the Bonds' indentures, including a cause pertaining to the acceleration of another substantial debt of the Company.

As of the date of the Financial Statements, the Company meets the contractual restrictions determined, with the Company's equity being approx. NIS 17 billion and the net financial debt to net assets ratio being approx. 29%.

**Note 19 – Loans from financial corporations (Cont.)**

**C. Details in respect of interest and linkage:**

| | | As of December 31 | As of December 31 | | | |
|---|---|---|---|---|---|---|
| | | 2018 | 2018 | | 2017 | |
| | Currency | Nominal interest | Par value | Book value | Par value | Book value |
| | | % | | NIS in millions | | NIS in millions |
| Overdrafts from banks (*) | Unlinked | 2.95 | | 1 | | - |
| Short-term loans from banks (*) | Unlinked | 2.25-2.6 | | 26 | | 28 |
| Short-term loans from banks | Foreign currency | 2.03 | | 20 | | 19 |
| Short-term loans from other credit providers | Index | 4.00 | | 1 | | 1 |
| Commercial paper | Unlinked | Bank of Israel + 0.3 | | 436 | | 582 |
| Bonds that are not convertible into shares | Index | 0.65-4.90 | 6,753 | 6,844 | 5,869 | 5,864 |
| Long-term loans from banks | Index | 3.77-5.80 | | 189 | | 210 |
| Long-term loans from banks (*) | Unlinked | .2.12-285 | | 28 | | 34 |
| Long-term loans from others | Index | 0.74-1.50 | | 950 | | 1,092 |
| Long-term loans from others (*) | Unlinked | 1.35 | | - | | 250 |
| Long-term loans from others | Linked to the Dollar | -3.166.0 | | 1,461 | | 1,170 |
| Total loans and credit from financial corporations | | | 6,753 | 9,956 | 5,869 | 9,250 |

(*) Some of the Shekel loans bear variable interest which is dependent on the Prime interest. The Prime interest rate as of December 31, 2018 and 2017 is 1.75% and 1.6%, respectively.

For details on loans that are secured by charges – see Note 30.

**Note 19 - Loans from financial corporations (Cont.)**

**D. Contractual restrictions and financial covenants in the Company:**

If certain conditions exist, as detailed in the loan agreements (primarily at the time of a change in the structure and the control in the Company, arrears in payments, receivership and a reduction in the value of the collateral), the loan providers are entitled to accelerate the loans. As of December 31, 2018, the total sum of credit for which the Company has undertaken the aforesaid terms and conditions amounted to approx. NIS 1,104 million. As of the date of the Financial Statements, the Company is in compliance with the contractual restrictions that have been set.

In addition, for a loan whose balance, as of the date of the Financial Statements, is in the sum of NIS 267 million, the LTV ratio is required, according to the agreement, to be lower than 40%. As of the date of the Financial Statements, the Company meets the contractual restriction that was set, with the actual LTV ratio being 21%.

**E. Changes in liabilities arising from financing activities:**

The table below specifies the changes in the Group's liabilities arising from financing activities, including both changes that arise from cash flows and non-cash changes. Liabilities arising from financing activities are liabilities in respect of which cash flows have been classified, or future cash flows will be classified, in the Statement of Cash Flows, as cash flows from financing activities.

| | Short-term credit from financial corporations | Long-term loans from financial corporations | Bonds | Total |
|---|---|---|---|---|
| | NIS in millions | | | |
| **Balance as of January 1, 2017** | 696 | 3,232 | 5,141 | 9,069 |
| Cash flows from financing activity (a) | (66) | (498) | 709 | 145 |
| Business combinations | - | 133 (b) | - | 133 |
| Linkage differentials | - | 2 | 10 | 12 |
| Exchange differences | - | (114) | - | (114) |
| Other changes | - | 1 | 4 | 5 |
| **Balance as of December 31, 2017** | 630 | 2,756 | 5,864 | 9,250 |
| Adjustment to opening balance due to effect of IFRS 9 | - | - | 6 | 6 |
| Cash flows from financing activity (a) | (147) | (241) | 907 | 519 |
| Linkage differentials | - | 10 | 63 | 73 |
| Exchange differences | - | 103 | - | 103 |
| Other changes | 1 | - | 4 | 5 |
| **Balance as of December 31, 2018** | 484 | 2,628 | 6,844 | 9,956 |

**Note 19 - Loans from financial corporations (Cont.)**

**E. Changes in liabilities arising from financing activities: (Cont.)**

(a) Cash flows from financing activities include the net cash flows presented in the Consolidated Statements of Cash Flows as cash flows that derive from financing activities.

(b) See Note 13D(2).

**Note 20 – Other liabilities**

"Other liabilities" includes primarily deposits in the sum of approx. NIS 60 million (2017 – approx. NIS 49 million) and employee benefits in the sum of NIS 8 million (2017 – NIS 6 million).

Employee benefits include post-employment benefits, other long-term benefits, benefits upon the termination of employment, short-term benefits, including due to wages and salary.

In respect of post-employment employee benefits, the Group has defined benefits plans, in respect of which it deposits amounts in appropriate severance pay funds and insurance policies. Moreover, the Group has a defined deposit plan in respect of some of its employees, with regard to whom Section 14 of the Severance Pay Law, 5723-1963 applies.

**Note 21 - Capital**

**A. The share capital and share rights as of December 31, 2018 and 2017:**

| | Authorized | | Issued and paid-up | |
|---|---|---|---|---|
| | As of December 31 | | As of December 31 | |
| | 2018 | 2017 | 2018 | 2017 |
| | NIS | NIS | NIS | NIS |
| Ordinary shares of par value NIS 0.1 | 12,750,150 | 12,750,150 | 12,127,276 | 12,127,276 |

Each fully paid-up ordinary share of par value NIS 0.1 grants the right to participate and vote at general meetings. Each shareholder will have one vote for every fully paid-up share he owns. All the shares have equal rights relating to the amounts of capital paid or credited as paid on their par value, and everything connected with distribution of dividend, bonus shares and any other distribution, repayment of capital and participation in the distribution of the Company's surplus assets upon liquidation.

**B. Dividend**:

The Company's Board discusses the issue of the distribution of a dividend at the Company (following the recommendation of the Finance Committee) on an annual basis. In such context, the desire and intention of the Company to share the Company's profits with its shareholders, versus the Company's being a development company on a significant scale and its investment needs in view of its existing activity and its future plans, were examined, while taking into account the gamut of business considerations.

In this framework, the Company's Board and the Finance Committee examine whether the dividend distribution meets the profit test and the solvency test set forth in Section 302 of the Companies Law. In addition, restrictions on distributions by the Company are examined, including the Company's undertaking to the trustee which includes restrictions on distributions by the Company, in connection with the indentures for the Company's Series B-F Bonds, see Notes19B(1)-(4), and in relation to some of the long-term loans, see Note 19B(7).

**Note 21 – Capital (Cont.)**

**C.** On March 21, 2017, the Company's Board decided upon the distribution of a NIS 480 million dividend (which reflects NIS 3.96 per share) for 2016, which was paid on May 10, 2017.

On March 20, 2018, the Company's Board decided upon the distribution of a NIS 520 million dividend (which reflects NIS 4.29 per share) for 2017, which was paid on May 2, 2018.

With respect to the decision of the Company's Board regarding the distribution of a dividend for 2018 in the sum of NIS 560 million after the date of the Statement of Financial Position, see Note 37A.

**Note 22 - Income**

**Composition of the income:**

| | For the year ended December 31 | | |
|---|---|---|---|
| | 2018 | 2017 | 2016 |
| | NIS in millions | NIS in millions | NIS in millions |
| Sales | 647 | 605 | 536 |
| Performance of work and services | 86 | 59 | 68 |
| Construction contracts | 17 | 16 | 41 |
| Franchise and other agreements | 8 | 44 | 15 |
| Total income from sales, work and services (*) | 758 | 724 | 660 |
| Rent, management and maintenance and senior housing fees | 2,063 | 1,868 | 1,745 |
| Total income | 2,821 | 2,592 | 2,405 |

(*) Including income from marketing alternative energy sources for 2018 in the sum of NIS 572 million (for 2017 and 2016 - NIS 556 million and NIS 505 million, respectively).

## Note 23 - Cost of income

**The composition:**

| | For the year ended December 31 | | |
|---|---|---|---|
| | **2018** | **2017** | **2016** |
| | **NIS in millions** | **NIS in millions** | **NIS in millions** |
| **A. According to the sources of income:** | | | |
| Sales | 402 | 358 | 295 |
| Performance of work and services | 75 | 61 | 72 |
| Construction contracts | 15 | 22 | 40 |
| Franchise and other agreements | 8 | 33 | 13 |
| | 500 | 474 | 420 |
| Rent, management and maintenance and senior housing fees | 543 | 484 | 445 |
| Total cost of income | 1,043 | 958 | 865 |
| **B. According to its components:** | | | |
| Gas and other materials consumed (*) | 316 | 294 | 260 |
| Labor and external work salary | 192 | 194 | 190 |
| Depreciation and amortization | 25 | 25 | 21 |
| Production expenses and others | 517 | 446 | 394 |
| | 1,050 | 959 | 865 |
| Net of increase/plus decrease in inventory of work in progress | - | - | 1 |
| Net of increase/plus decrease in inventory of finished products | (7) | (1) | (1) |
| | 1,043 | 958 | 865 |

(*) The purchases of gas from Oil Refineries Ashdod Ltd. and from Oil Refineries Ltd. are above 10% of the acquisitions.

## Note 24 - Sales and marketing expenses

**The composition:**

| | For the year ended December 31 | | |
|---|---|---|---|
| | 2018 | 2017 | 2016 |
| | NIS in millions | NIS in millions | NIS in millions |
| Wages, salaries and related expenses | 81 | 78 | 73 |
| Advertising | 50 | 48 | 34 |
| Depreciation and amortization | 35 | 33 | 31 |
| Maintenance of buildings and facilities | 5 | 5 | 5 |
| Rent and municipal taxes | 4 | 4 | 4 |
| Haulage and maintenance of commercial motor vehicles | 11 | 10 | 11 |
| Other sales and marketing expenses | 14 | 14 | 14 |
| | 200 | 192 | 172 |

## Note 25 - General & administrative expenses

**The composition:**

| | For the year ended December 31 | | |
|---|---|---|---|
| | 2018 | 2017 | 2016 |
| | NIS in millions | NIS in millions | NIS in millions |
| Management fees, wages, salaries and related expenses (*) | 42 | 39 | 34 |
| Consultancy, legal and audit fees | 39 | 37 | 35 |
| Provision for doubtful and lost debts | 6 | 3 | 2 |
| Depreciation and amortization | 8 | 6 | 8 |
| Other general and administrative expenses | 28 | 29 | 25 |
| | 123 | 114 | 104 |

(*) For details in respect of transactions with related and interested parties – see Note 35C.

## Note 26 - Other income

"Other income" includes primarily dividends received from investments in financial assets (Leumi and Leumi Card) in the sum of NIS 90 million (in the years 2017 and 2016 – NIS 33 million and NIS 10 million, respectively), in the year 2017 includes income from the Visa Europe transaction in the sum of approx. NIS 30 million (see Note 11B(2), and income from indemnification by the insurance company for the Texas storm damage in the sum of NIS 64 million (see Note 13D(1)).

## Note 27 - Financing revenues and expenses

**The composition:**

| | For the year ended December 31 | | |
|---|---|---|---|
| | 2018 | 2017 | 2016 |
| | NIS in millions | NIS in millions | NIS in millions |
| **Financing revenues** | | | |
| Revenues from interest on loans and receivables | 12 | 8 | 15 |
| Financing revenues from a financial asset in respect of franchise arrangement | 3 | 3 | 2 |
| Profit from a change in exchange rates, net | - | - | 3 |
| Revenues from interest on deposits in banks | 2 | 2 | 2 |
| Classification as profit or loss of profits that were recognized in other comprehensive income upon the disposition of financial assets (see Note 11(a)) | - | 81 | 26 |
| Other financing revenues | - | - | 1 |
| Financing revenues carried to profit and loss | 17 | 94 | 49 |
| **Financing expenses** | | | |
| Financing expenses on loans and liabilities | 100 | 92 | 117 |
| Financing expenses on bonds | 169 | 107 | 86 |
| Miscellaneous bank expenses and charges | 14 | 11 | 8 |
| Loss from change in exchange rates, net | 1 | 1 | - |
| Linkage on deposits from customers | 8 | 2 | (1) |
| Other financing expenses | 10 | 9 | 5 |
| Financing expenses | 302 | 222 | 215 |
| Net of capitalized credit costs | (44) | (38) | (56) |
| Financing expenses carried to the income statement | 258 | 184 | 159 |
| Net financing expenses carried to the income statement | 241 | 90 | 110 |

**Note 28 – Taxes on income**

**A. Details in respect of the tax environment in which the Group operates:**

**(1) Amendments to the Income Tax Ordinance and the Land Appreciation Tax Law**

**(a)** On December 29, 2016, the Economic Arrangements Law (Legislative Amendments to Achieve the Budget Targets for 2017 and 2018), 5777-2016 was published in the Official Gazette, in the framework of which the corporate tax rate will be reduced from 25% to 24% in 2017 on income generated or accrued commencing January 1, 2017 and shall continue to be reduced to 23% in 2018 forth on income generated or accrued commencing January 1, 2018.

As a result of the said legislation, there is a decrease in the deferred tax liabilities of the Company as of December 31, 2016 in the sum of approx. NIS 420 million and a decrease in the balances of the deferred tax assets in the sum of NIS 12 million which was recorded against other comprehensive income for 2016 in the sum of approx. NIS 408 million, of which a sum of approx. NIS 393 million was recorded against tax income in 2016.

**(b)** In August 2013, the “Arrangements Law” (the “**Law**”) was published in the Official Gazette in which context Section 100A1 of the Income Ordinance was added, determining that revaluation profits will be taxable, based on a mechanism of a notional sale and purchase of an asset at any time for which a revaluation thereof was performed, from which revaluation profits were also distributed. Accordingly, a parallel provision was set forth in the Land Taxation Law (Appreciation and Purchase) with respect to appreciation tax on a right in land or a right in a land association for which a distribution from revaluation profits was recorded in the Company’s financial statements, as if the right was sold on the date of distribution of the revaluation profits, and re-purchased on the same day.

The applicability provisions determine that they shall apply to assets outside of Israel on the effective date of regulations to be promulgated by the Minister of Finance, and provisions shall be set for the avoidance of double taxation within the meaning thereof in Section 200 of the Income Tax Ordinance. Furthermore, the definition of “Revaluation Profits” determined that they are “surpluses not subject to corporate tax of the type determined by the Minister of Finance”. As of the date of approval of these Financial Statements, not such regulations have been published.

In view of the manner in which the decision on dividend distribution is made at the Company, as stated in Note 21B, such legislation has no significant tax implications for the Company.

**(2)** The Company and a subsidiary have a holding (90%-99%) in American partnerships, which hold real property. The profits (losses) of the American partnerships from the rental of the real properties and from the sale thereof are attributable directly to the partners, in accordance with their shares in the capital, because under American tax law, a partnership which has been registered in the U.S. is considered to be transparent for tax purposes.

Accordingly, the profits (losses) of the American partnerships in which it serves as a limited partner will be attributed to the Group and it will accordingly be liable for tax in the U.S. in respect of the profits, attributed thereto as aforesaid in accordance with the Federal corporate tax rate (at a rate of 21%) and Texas state tax (whose rate on December 31, 2018 was 0.75% of the “taxable margin”, as defined in the law), which constitutes an expense for the purposes of the calculation of the Federal tax. In addition, under certain circumstances, a "branch tax" at the rate of 12.5% may be levied on part of the profits of the partnerships (even if not yet actually distributed). If such profits are reinvested for business in the U.S. and subject to compliance with additional conditions, the "branch tax" may be deferred.

In a similar manner, the general partners in the American partnerships will be liable for tax in the U.S. in respect of their share (1%) of the profits (losses) from the rental of the real properties and/or from the sale thereof, in accordance with the tax rates that are mentioned above (with the exclusion of "branch tax").

**Note 28 – Taxes on income (Cont.)**

**A. Details in respect of the tax environment in which the Group operates: (Cont.)**

**(2) (Cont.)**

In accordance with the provisions of Section 63 of the Ordinance, the limited partners (the Company and its subsidiary), will be liable for corporate tax in Israel in respect of their share of the profits from the rental of the land in the U.S. and in the real capital gain that is derived from their sale by the American partnerships.

In the case of tax payable in the U.S., in respect of which it is not possible to obtain a tax credit in Israel in the tax year in which it was paid, *inter alia*, by reason of losses for tax purposes incurred by the subsidiary - a credit may be obtained in respect thereof (in adjusted values, in accordance with the rate of the rise in the CPI) against the tax imposed on the subsidiary in Israel in respect of revenues from lease overseas in the 5 subsequent years.

**(3)** The Company has a holding (100%) in U.S. subsidiaries that are liable for tax in the U.S.. The subsidiaries are liable for Federal Tax rate on the companies' current income and capital gains from the sale of the real properties of 21%, and for Texas state tax.

On January 1, 2018, a U.S. corporate tax reform took effect, after its enactment was in fact completed by its approval by the U.S. House of Representatives and Senate and signing by the President of the United States in December 2017. The main change affecting the Group was the decrease of the federal tax rate to 21% from tax year 2018 forth, instead of 35% until the end of tax year 2017. In view of the aforesaid, the Company reduced in the year 2017 its deferred tax liabilities by approx. NIS 15 million.

**B. Tax revenues (expenses) on income recognized in the income statement:**

| | For the year ended December 31 | | |
|---|---|---|---|
| | 2018 | 2017 | 2016 |
| | NIS in millions | NIS in millions | NIS in millions |
| **Current tax revenues (expenses)** | | | |
| For the current period | (141) | (176) | (171) |
| Net taxes in respect of previous years | (110) | 8 | 4 |
| | (251) | (168) | (167) |
| **Deferred tax income (expenses)** | (42) | (240) | 118 |
| **Total expenses of taxes on income** | (293) | (408) | (49) |

**Note 28 – Taxes on income (Cont.)**

**C. Taxes on income in respect of the components of other comprehensive income:**

| | 2018 | | | 2017 | | | 2016 | | |
|---|---|---|---|---|---|---|---|---|---|
| | Amounts before tax | Tax income (*) | Amounts net of tax | Amounts before tax | Tax income (expenses) (*) | Amounts net of tax | Amounts before tax | Tax income (expenses) (*) | Amounts net of tax |
| | NIS in millions | | | | | | | | |
| Translation differences from foreign operations | 95 | - | 95 | (114) | - | (114) | (11) | - | (11) |
| Change in the fair value of financial assets | - | 11 | 11 | 269 | (65) | 204 | 134 | (18) | 116 |
| Amounts that were carried to the income statement from disposition of financial assets | - | - | - | (81) | 19 | (62) | (26) | 6 | (20) |
| Total other comprehensive income | 95 | 11 | 106 | 74 | (46) | 28 | 97 | (12) | 85 |

(*) The deferred taxes have been calculated in accordance with a tax rate of 23% (in 2017 according to 23% and in 2016 according to 23%-24%).

**Note 28 – Taxes on income (Cont.)**

**D. Compatibility between the theoretical tax on the income before income taxes and the tax expenses:**

| | For the year ended December 31 | | |
|---|---|---|---|
| | 2018 | 2017 | 2016 |
| | NIS in millions | NIS in millions | NIS in millions |
| Income before income taxes | 1,514 | 1,856 | 1,866 |
| The Company's principle tax rate | 23% | 24% | 25% |
| Tax calculated at the Company's principle tax rate | 348 | 445 | 467 |
| **Addition (saving) in the tax liability in respect of:** | | | |
| Different tax rates and laws in subsidiaries that operate outside of Israel | 4 | (16) | (13) |
| Net of tax calculated in respect of the Company's share in the losses of associates accounted for by the equity method | 2 | 1 | 2 |
| Exempt income | (30) | (7) | (3) |
| Expenses not recognized | 1 | 1 | 2 |
| Company's share in partnerships | (1) | (1) | (1) |
| Utilization and creation of deferred taxes in respect of losses and benefits from previous years, in respect of which deferred taxes were not recorded | (140) | (3) | (11) |
| Losses and benefits for tax purposes from the period in respect of which deferred taxes were not recorded | 11 | 21 | 6 |
| Taxes in respect of previous years | 110 | (7) | (4) |
| Differences in the definition of capital, assets and expenses for tax purposes and others | (10) | (2) | 1 |
| Effect of the change in the statutory tax rate | - | (24) | (393) |
| Other differences | (2) | - | (4) |
| **Expenses of taxes on income** | 293 | 408 | 49 |

**Note 28 – Taxes on income (Cont.)**

**E. Deferred tax assets and liabilities:**

**(1) Deferred tax assets and liabilities that have been recognized**

The deferred taxes in respect of companies in Israel have been calculated in accordance with the tax rates that are expected to apply at the time of the reversal, as detailed above. Deferred taxes in respect of subsidiaries that operate outside of Israel have been calculated in accordance with the relevant tax rates in each country.

The deferred tax assets and liabilities are attributed to the following items:

| | Real estate and fixed assets | Employee benefits | Financial instruments (1) | Deductions and losses to be carried forward for tax purposes | Others (2) | Total |
|---|---|---|---|---|---|---|
| | NIS in millions | | | | | |
| **Deferred tax as of January 1, 2017** | (2,933) | 5 | (106) | 131 | 10 | (2,893) |
| Changes carried to profit and loss | (246) | - | (6) | (7) | 1 | (258) |
| Changes carried to other comprehensive income | - | - | (46) | - | - | (46) |
| Effect of the change in the tax rate carried to profit and loss | 28 | - | - | (10) | - | 18 |
| **Deferred tax as of December 31, 2017** | (3,151) | 5 | (158) | 114 | 11 | (3,179) |
| Changes carried to profit and loss | (205) | - | 15 | 141 | 7 | (42) |
| Changes carried to other comprehensive income | - | - | 11 | - | - | 11 |
| Adjustment to opening balance due to effect of IFRS 9 | - | - | - | - | 1 | 1 |
| **Deferred tax as of December 31, 2018** | (3,356) | 5 | (132) | 255 | 19 | (3,209) |

(1) Primarily for financial assets at fair value through other comprehensive income and financial asset – receivables in respect of franchise arrangement.

(2) Primarily doubtful debts and linkage differentials on deposits from customers.

(*) The deferred taxes have been calculated according to a 23% tax rate. For details regarding changes in the tax rate in previous years – see Note 28A(1)A).

**Note 28 – Taxes on income (Cont.)**

**E. Deferred tax assets and liabilities: (Cont.)**

**(2) Deferred tax assets that have not been recognized**

Deferred taxes not recognized in respect of the following items:

| | As of December 31 | |
|---|---|---|
| | 2018 | 2017 |
| | NIS in millions | NIS in millions |
| Losses for tax purposes | 116 | 107 |
| Capital loss for tax purposes | 43 | 152 |
| Real difference from securities | 7 | 7 |
| | 166 | 266 |

**(3) Losses and deductions for tax purposes that are available to be carried forward to the coming years**

**(a)** Current business losses and deductions from a future tax liability according to an assessment agreement for tax purposes of the Company and consolidated companies, which are carried forward to the following year, amount as of December 31, 2018 to approx. NIS 1,095 million (December 31, 2017 – approx. NIS 512 million).

As of December 31, 2018, consolidated companies have recorded a deferred tax asset of NIS 223 million in respect of accumulated business losses (December 31, 2017 – NIS 88 million) in accordance with the management's evaluation that there is a high level of confidence that these losses and deductions will be realized in the coming years.

**(b)** The Company and consolidated companies have accumulated capital losses for tax purposes in the sum of approx. NIS 184 million (December 31, 2017 – approx. NIS 264 million). The Company and consolidated companies recorded deferred tax assets in the sum of NIS 32 million in respect of accumulated capital losses (December 31, 2017 – NIS 26 million).

**(c)** According to the existing tax laws in Israel, there is no time restriction for the exploitation of losses for tax purposes, or on the exploitation of the deductible temporary differences. Deferred tax assets have not been recognized in respect of such losses and differences, in cases where it is not expected that there will be sufficient chargeable income in the coming years against which it will be possible to exploit the tax benefits.

**(d)** The Group does not create deferred taxes that relate to investments in consolidated companies in respect of which the decision as to the disposition thereof is in the Group's hands whenever there is no decision to realize them in the foreseeable future.

## Note 28 – Taxes on income (Cont.)

### F. Tax assessments:

The Company and some of the consolidated companies have final tax assessments up to and including the 2016 tax year.

On December 12, 2018, a settlement agreement was signed between the Company and Canit Hashalom Investments Ltd., a wholly-owned subsidiary of the Company, with the Israel Tax Authority in respect of tax assessments pursuant to Section 152(B) of the Income Tax Ordinance for the years 2011-2014, with respect to which the Company filed an appeal with the Court, and also in respect of the years 2015-2016 (the "**Settlement Agreement**"). As part of the Settlement Agreement, the Company has paid NIS 176 million, most of which will be returned to the Company in the coming years as a deduction from future tax liability (timing differences). The Settlement Agreement has no material effect on the Company's financial results.

Some of the consolidated companies have final tax assessments up to and including the tax years 2013-2015.

Save for the above mentioned companies, the other Group companies have final tax assessments up to and including the years 2013-2014, in the framework of Section 145(a)(2) of the Income Tax Ordinance (Prescription).

## Note 29 – Engagements

**The consolidated companies have engagements and liabilities as of the date of the Statement of Financial Position, as follows:**

### A. Material engagements:

| | | NIS in millions |
|---|---|---|
| **(1)** | For the purchase of fixed assets | 1 |
| | For the performance of projects | 1,059 |
| | For rentals and leases (*) | 49 |
| | For operating leasing agreements for motor vehicles | 5 |

| | | |
|---|---|---|
| (*) | The payment due dates of rental and lease liabilities are as follows: | |
| | 2019 | 14 |
| | 2020 | 12 |
| | 2021 | 3 |
| | 2022 | 2 |
| | 2023 forth | 18 |
| | | 49 |

**(2)** With respect to the engagements with related and interested parties, see Note 35.

**Note 29 – Engagements (Cont.)**

**B. Additional engagements:**

**(1)** The Company and its subsidiaries engaged with OPC Rotem Ltd. ("**OPC**"), a private electricity producer, in an agreement to purchase electricity. In addition, the companies of the Group engaged in a parallel agreement between them, which regulates the relationship between the companies of the Group in relation to the aforesaid agreement. Pursuant to the agreement, OPC shall sell electricity to the companies of the Group in the volume that is set forth in the agreement, in consideration for a tariff which varies according to actual consumption which is based on the tariffs of the Israel Electric Corporation Ltd. (the "**IEC**"), net of various discount rates determined in the agreement, which depend on the companies' volumes of consumption. The agreement is effective for a 15-year period, commencing from July 2013. The agreement sets forth special conditions that allow the parties to terminate it by giving an advance notice. In the event that OPC's power plant does not work and does not supply electricity for any reason whatsoever, electricity shall be supplied directly from the IEC. The agreement sets forth maximum and minimum volumes of electricity consumption by the companies of the Group. In the event of failure to meet the minimum volumes, the discount shall be gradually reduced.
The Group's companies reserve the right to purchase 100 megawatt hour more, in the event of the construction of an additional power plant by OPC's parent company.

**(2)** In July 2013, Supergas Natural Ltd. ("**Supergas Natural**"), a consolidated company of Supergas, signed an agreement with the partners in the Tamar holding for the supply of natural gas for a period of 5 years, whereby Supergas Natural shall purchase natural gas from the sellers for the marketing thereof to its customers. Due to non-fulfillment of conditions that were defined in the agreement, Supergas Natural is not subject to an obligation to purchase natural gas.

During Q1/2018, Supergas Natural signed agreements with a third party for the purchase of natural gas in the scope of approx. NIS 800 million for the purpose of marketing thereof to its customers.

The supply period is expected to begin during 2020 for a period of about 7 years. The agreements include mechanisms for a minimum purchase commitment and compensation as customary in similar transactions.

**(3)** Investee companies of Supergas (50%), hold licenses for the establishment and operation of a natural gas distribution network in the center of Israel (from November 2019) and in the Hadera and Valleys area (from April 2013) and for operation thereof for a 25-year period. Pursuant to the terms of the licenses, the companies are required to invest approx. NIS 160 million in the establishment of the distribution network in the center of Israel and approx. NIS 218 million in the Hadera and Valleys area, according to the milestones determined in the licenses. Until December 31, 2018 a total amount of approx. NIS 175 million has been invested. According to the terms and conditions of the licenses, the companies will receive their income from one-time connection fees and from a distribution fee tariff, as specified in the license. The companies have commenced transmitting natural gas to customers and are working to complete the planning of segments and develop the setup of the network. In view of bureaucratic and regulatory difficulties which are delaying the progress of the network's rollout and the connection of consumers, and in view of applications by the distribution companies to update the conditions of the license and the timetables, in May 2018, the Ministry of Energy published a call for acceleration of the rollout of the distribution network, aiming to assist the distribution companies in completing the rollout of the distribution network. The distribution companies have accepted the call and signed agreements for an outline for the development of the distribution networks, and, at the same time, are continuing to act for an update of the conditions of the license. In order to meet the license conditions, the investee companies of Supergas provided unconditional autonomous guarantees in favor of the State of Israel in the sum total of approx. NIS 18 million, which will be valid for the entire term of the license and for 6 months and 24 months, respectively, after the license end date and termination date. For the purpose of provision of the guarantee, Supergas provided a guarantee to the investee companies for its relative share (50%).

**Note 29 – Engagements (Cont.)**

**B. Additional engagements: (Cont.)**

**(4)** Supergas engaged with a third party company in an agreement for cooperation respect to natural gas, in which it was agreed, *inter alia*, that: (1) The third party company would be entitled to 30% of the profit from the marketing of the natural gas of Supergas to be supplied through the distribution network to customers in areas in which Supergas and the third party company have licenses to set up and operate a natural gas distribution network; (2) a company would be established which would act as the contractor to set up the distribution networks which would be held 70% by the third party company and 30% by Supergas.

**(5)** On May 20, 2015, a consolidated company, Ahuzat Bayit Ra'anana – Retirement Home Ltd., entered into a trust agreement with a trust company, whereby it will serve as the trustee of the residents of the retirement home for the purpose of registration of the mortgages in their favor. Pursuant to the agreement, the consolidated company registered a first ranking mortgage in favor of the trust company at the Land Registry, on a majority of the sub-parcels that constitute the land of the retirement home. The consolidated company is acting to complete the registration of the mortgage in favor of the trust company on all of the sub-parcels of the retirement home.

**(6)** On November 16, 2014 Ahuzat Bayit Ra'anana – Retirement Home Ltd. ("**Ahuzat Bayit**") entered into a contract with former controlling shareholders thereof to separate the past activities (the "**Separation of Past Activities Contract**"), in which its former controlling shareholders undertook to indemnify Ahuzat Bayit for all Past Debts, such that Ahuzat Bayit will not be required to itself bear any Past Debt, and that Ahuzat Bayit shall transfer to its former controlling shareholders assets deriving from past activities.

For this purpose, Past Debts – any liability of any kind whatsoever which applies to Ahuzat Bayit and which derives, directly or indirectly, from the known debts, the existing legal proceedings and the additional debts, without exception, and including legal costs, consultants' costs and any additional liability payment and/or expense relating thereto, and all with the exception of: (1) Debts in connection with the land, the "Ahuzat Bayit" senior home business and the "Park Mall" shopping center, directly and/or indirectly, whether the cause thereof precedes or is subsequent to the date of signing of the Separation of Past Activities Contract; (2) Undertakings for payment of loans/capital notes of any kind whatsoever, including banks and other third parties – and all as provided in the contract. It is clarified that in the context of transfer of control of Ahuzat Bayit, an investee company of the Company and Ahuzat Bayit received a letter of undertaking from the former controlling shareholders, whereby the liability of the former controlling shareholders for the past activities in Ahuzat Bayit, remains in effect.

To secure the said indemnity, the former controlling shareholders placed a deposit in trust, which, as of the date of signing of the financial statements, is in the sum of approx. NIS 5.3 million.

**(7)** On April 10, 2018, notice was received by Zero Waste Ltd. ("**Zero Waste**"), a corporation held by GES, in equal shares with Shikun & Binui Ltd. ("**Shikun & Binui**"), whereby Zero Waste had been elected as the winner in a BOT tender for the planning, financing, construction and operation of a facility for municipal waste sorting and recycling and energy production (the "**Project**"), published by the Ministry of Finance and the Ministry of Environmental Protection. The Project will be built in the area of the Dan Region Wastewater Treatment Plant (the "*Shafdan*") in Rishon LeZion, and its cost during the construction period is estimated at approx. NIS 750 million. On May 31, 2018, Zero Waste signed a franchise agreement with the State. As of such date, Zero Waste has begun acting for the fulfillment of its obligations under the franchise agreement, including the accomplishment of financial closing at the lapse of 15 months as of the signing day.

GES will co-hold, with a subsidiary of Shikun & Binui, equal shares of the rights in the construction contractor that will carry out the Project's construction work, and will also co-hold, with Shikun & Binui, equal shares of the contractor that will operate the Project.

**Note 29 – Engagements (Cont.)**

**B. Additional engagements: (Cont.)**

**(7) (Cont.)**

The execution of the Project is subject to the completion of a financial closing of the Project, as part of which Zero Waste will be required, *inter alia*, to obtain the financing required for the execution of the Project. The overall franchise term of the Project is up to 29.5 years, of which a period of up to 15 months is for of the financial closing and a period of 40 months is for completion of the Project's construction work (including the facility's trial run). The costs in respect of the execution of the Project in the period thus far are not material.

The Company is a guarantor for the fulfillment of GES's obligations vis-à-vis Shikun & Binui, subject to and as provided in the shareholders agreement between GES and Shikun & Binui with respect to Zero Waste. Such guarantee will expire upon completion of the Project's construction and receipt of the commercial operation permit therefor.

In July 2018, Zero Waste received the petition of another group that contended in the same tender, in which petition the Jerusalem District Court was moved, *inter alia*, to revoke the Tender Committee's decision to choose Zero Waste as the winner of the tender and determine that the other group is the winner of the tender, or alternatively remand the matter to the Tender Committee for examination of Zero Waste's compliance with the requirements of the tender. On February 19, 2019, the Court's decision was given, denying the petition with no order for costs.

**(8) Azrieli Holon Center**

The Group, via Canit Hashalom, is the owner of leaseholds in a reserve of land of a total area of approx. 30,000 sqm in the East Holon Industrial Area (in this section: the "**Land Reserve**") under an agreement that was signed between the Municipality of Holon and Canit Hashalom on June 5, 2008 (in this section: the "**Agreement**") and approved by the Minster of the Interior in December 2008. Within the framework of the Agreement, Canit Hashalom made guarantees available to the Economic Company for the Development of Holon Ltd., which is intended to ensure the compliance with Canit Hashalom's undertakings under the Agreement. As of the date of the financial statement, there are no guarantees in favor of the Municipality of Holon.

The entire Land Reserve is owned by the Municipality of Holon, without any known charges or mortgages. In accordance with the Agreement the project is for the construction of a business park (with no more than four sub-stages), including buildings for hi-tech offices, display halls and retail, service areas and parking areas as well as for additional uses (the "**Project**"). The Project was built and is operated as an income-producing property (for rental) by way of a joint venture, where the material terms of the transaction are as follows:

**(a)** The Municipality of Holon is leasing to Canit Hashalom, in accordance with the Agreement, for a period of 99 years with an option for an additional 99 years for a payment, 83% of the areas and land of the Project.

**(b)** The Project is managed and operated by the Company as an income-producing property that is held jointly by the two parties, where the areas of the Project are leased as a common reserve for the two parties. The areas are leased through a management company wholly owned by the Company, and the division of the rent is carried out using a mechanism that has been agreed by the two parties.

**(c)** The Project is managed by a management company. Management is executed on the basis of cost +15%, which constitute the fees of the management company.

**Note 29 – Engagements (Cont.)**

**B. Additional engagements: (Cont.)**

**(8) Azrieli Holon Center (Cont.)**

**(d)** The Agreement sets various restrictions on the transfer of rights in areas in the Project and/or in the rights and undertakings of Canit Hashalom thereupon. It is further determined in the Agreement that the transfer of shares, including by way of a public offering, in shares of Canit Hashalom in an amount of up to 25% will be permitted. It is further clarified that the provisions relating the transfer of rights and a change in the ownership structure will not apply to the parent company or to a subsidiary or an affiliate of Canit Hashalom.

**(e)** The Group treats this Project as a joint operation.

## Note 30 - Charges and guarantees

### A. Fixed and floating charges:

| | As of December 31, | | |
|---|---|---|---|
| | 2018 | 2017 | |
| | NIS in millions | NIS in millions | Secured by |
| Short-term credit from banks | 17 | 10 | In a consolidated company a floating charge on credit cards. In another consolidated company, floating charges on all the assets of the consolidated company and fixed charges on shares of an investee company thereof, goodwill and an asset of its investee company. In addition, fixed and floating charges have been registered on assets of consolidated companies thereof, including on the rights existing in any agreements. |
| Long-term loans from banks and others (including accumulated interest presented in short-term) | 2,641 | 2,517 | A charge on the rights to receive monies in respect of investment property of the Company and of some of the investee companies. The book value of the pledged assets – approx. NIS 7 billion.<br><br>In a consolidated company, a floating charge was registered on all the assets of a consolidated company thereof, including rights deriving therefrom and a fixed charge on shares of an investee company thereof, insurance rights and rights deriving from an asset of a consolidated company. The value of the pledged asset of the consolidated company is approx. NIS 0.1 billion.<br><br>In another consolidated company, a fixed charge on the consolidated company’s assets, including real properties, deposits in banks and revenues from customers. The value of the pledged real properties of the consolidated company is approx. NIS 0.3 billion. |
| Bonds (including accumulated interest presented in short-term) | 327 | 362 | In a consolidated company, the bonds are collateralized by a first ranking floating charge, in an unlimited amount, on all of the assets of the consolidated company. In addition, the investee company has created a first ranking fixed charge in an unlimited amount over all shares of a consolidated company thereof owned and held thereby, including the rights that derive from such shares. The value of the pledged assets of the consolidated company is approx. NIS 0.25 billion. |

**Note 30 - Charges and guarantees (Cont.)**

**A. Fixed and floating charges: (Cont.)**

| | As of December 31, | | |
|---|---|---|---|
| | 2018 | 2017 | |
| | NIS in millions | NIS in millions | Secured by |
| Senior housing residents' deposits | 819 | 664 | On the date of entry of residents, consolidated companies registered caveat notes in favor of the residents or the depositors, the purpose of which is to ensure repayment of the balance of the deposit. At present, the property is in the process of condominium registration. Upon completion of the process, the consolidated companies will register a mortgage for every resident on his apartment, *in lieu* of the caveat note.<br><br>Pursuant to the provisions of the Senior Housing Law which took effect on June 3, 2015, the consolidated companies are required to provide the residents with collateral. The options for collateral include, *inter alia*, a bank guarantee or a mortgage. The consolidated companies are acting, as stated, to register mortgages in favor of the residents. Insofar as the condominium registration process is not completed and it is not possible to register mortgages in favor of the residents, the consolidated companies will examine additional options as prescribed by the law.<br><br>In an additional consolidated company, a first-ranking mortgage was registered in favor of the residents at the Land Registry on most of the sub-plots that comprise the land of the senior home.<br><br>In addition, to secure some of the undertakings of the consolidated company in respect of deposits, caveats were registered at the Land Registry in favor of the residents. |

(*) The Company committed to banks, financial institutions and in the indentures to the bonds that it would not create floating charges over its entire assets. The Company may create a floating charge as aforesaid, provided that concurrently with the creation thereof, it will create a floating charge to the benefit of the lender as well. The Company also committed, irrevocably, to a bank that it had not created and will not create a floating charge over its entire property and assets, whether they are owned thereby or will be owned thereby in the future, including over the goodwill and share capital thereof, and it also committed towards another bank not to commit in any manner to create a floating charge as aforesaid, without the advance written agreement of the bank.

(**) In addition, to secure the conditions relating to a certificate of approval of the Investment Center, a floating charge was registered at a consolidated company on all of the machines, equipment, facilities and land thereof in favor of the State of Israel.

**Note 30 - Charges and guarantees (Cont.)**

**B. The Company and consolidated companies have contingent liabilities:**

| | | As of December 31 | |
|---|---|---|---|
| | | **2018** | **2017** |
| | | **NIS in millions** | **NIS in millions** |
| **(1)** | Financial guarantees to banks extended by a consolidated company for a consolidated company thereof | 75 | 75 |
| **(2)** | Performance and other guarantees: | | |
| | - Performance guarantees for customers and others, including tender guarantees | 63(**) | 52 |
| | - Guarantees to authorities - of which sum of approx. NIS 87 million due to demands for betterment levies. | 142 | 131 |
| **(3)** | Guarantees to lessor in respect of usage rights for LTC units. | 1 | 1 |
| **(4)** | Guarantees for undertakings in respect of tenants. | 6 | 5 |
| **(5)** | A guarantee extended by a consolidated company in favor of a consolidated company thereof in respect of its liabilities to banks. | 27 | 34 |
| **(6)** | A guarantee extended by a consolidated company in favor of a consolidated company thereof in respect of its liabilities to its customers. | 19 | 24 |
| **(7)** | Guarantees and letters of indemnification given by a consolidated company to banks financing projects of former controlling shareholders of the consolidated company, which shall remain in effect until the completion of such projects. For such guarantees, the consolidated company received an indemnity from the former controlling shareholders (see Note29B(6)). | 4 | 3 |

(*) In addition to guarantees given by the Company and an investee company to consolidated limited partnerships thereof overseas and to consolidated companies thereof overseas, for their liabilities to financial corporations, which are enforceable only in several specific cases defined in the loan agreements (Bad Boy).

(**) On the Company’s guarantee in respect of a BOT project for the treatment of solid municipal waste in the Dan Region Wastewater Treatment Plant (the “*Shafdan*”), see Note 29B(7).

**Note 31 - Contingent liabilities**

**A. Class actions and claims in respect of which motions for class action certification were filed:**

| Parties | Amount of claim | Nature of claim | Prospects of claim |
|---|---|---|---|
| 1. Claim against the Company | A claim in the sum total of approx. NIS 58 million (estimate). | A motion for the certification of a class action filed in May 2018, concerning claims pertaining to an alleged violation of the provisions of the Equal Rights for Persons with Disabilities Law, 5758-1998 and regulations promulgated thereunder. | A this initial and preliminary stage, in reliance on its legal counsel, the Company is unable to estimate the prospects of the motion being granted. However, it is noted in this respect that: (a) Other class action certification motions that were previously filed against the Company with respect to such issues indicate that the Company is meticulous in its compliance with the provisions of the law in this context; and (b) Past experience indicates that chances of the certification motion being fully granted are lower than 50%, and certainly much lower than the chance that the certification motion will eventually be granted in the amounts sued. |
| 2. Claim against three gas companies, including Supergas | A claim and a motion for class action certification filed in November 2016. Amongst the remedies sought is the demand to reimburse amounts collected, allegedly in excess, from the customers of the defendant companies. The motion does not state an amount. | A claim and a motion for the certification of a class action alleging that Supergas and the other gas companies allegedly violated the Restrictive Trade Practices Law, by being parties to a restrictive arrangement, and the existence of a cartel between Supergas and other gas companies. | In the Company’s estimation, based on the estimation of Supergas, in reliance on its legal counsel, the chances of the motion for class action certification are less than 50%. |

**Note 31 - Contingent liabilities (Cont.)**

**B. Other actions:**

| Parties | Amount of claim | Nature of claim | Prospects of claim |
|---|---|---|---|
| 1. Indictment against Supergas and directors thereof | Criminal | In October 2011, the Municipality of Kiryat Ata brought two proceedings against Supergas in the Krayot Court of Local Affairs – (1) An indictment under the Business Licensing Law in respect of the operation of the gas farm in Kiryat Ata without a business license. This proceeding was brought both against Supergas and against directors thereof. (2) A motion for the issuance of an order for the cessation of work in a business, which seeks for an order to be issued against Supergas, ordering it to immediately discontinue the gas farm's activity due to the absence of a business license. This motion was filed as an interim motion in the framework of the aforementioned indictment. | As pertains to the proceeding of the motion for an cessation of work order – A court decision, within which the Municipality's motion was denied, was issued in January 2012. As pertains to the indictment proceeding, in November 2017, April and October 2018 court hearings were held and additional hearings are scheduled to take place over the course of 2019. In the Company's estimation, in reliance on estimation by Supergas's management, at this stage and in view of the type of the proceeding, the chances thereof cannot be estimated. |

**Note 31 - Contingent liabilities (Cont.)**

**B. Other actions: (Cont.)**

| The parties | Amount of claim | Nature of claim | Prospects of claim |
|---|---|---|---|
| 2. Claim against Supergas and two other gas companies | Approx. NIS 71 million against all defendants. | In March 2017, a pecuniary claim was filed against Supergas and two other gas companies with respect to alleged violations of the Trade Practices Law and a violation of various provisions of the State Economy Arrangements Law (Legislation Amendments), 5749-1989. | At the request of the other gas companies that are sued in this proceeding, the court has issued a stay of proceedings in this case.<br><br>In the Company's estimation, based on Supergas's estimation, in reliance on its legal counsel, Supergas holds significant proof for the claim against it to be rejected. However, in view of the preliminary stage of the proceeding, the chances thereof cannot be estimated at this stage. |
| 3. Demand for payment by Supergas | Demand in the total sum of approx. NIS 117.2 million. | In the years 2011-2012, the Local Committee of the of Municipality of Kiryat Ata sent betterment levy assessments in respect of the approval of NOP 32/C, following Supergas's application for a building permit for Supergas's gas facility complex in Kiryat Ata. | On November 1, 2018, a judgment was handed down on the appeal that had been filed with the Supreme Court by the Municipality of Kiryat Ata from the decision of the Court for Administrative Affairs on the betterment levy charge and on the payment of compensation under Section 197 of the Planning and Building Law. According to the judgment, the betterment levy the Municipality sought from the gas companies and the compensation under Section 197 of the Planning and Building Law sought by the gas companies offset each other, such that no pecuniary obligation will be imposed on any of the parties.<br>In view of the aforesaid, Supergas estimates that this proceeding has been concluded. However, insofar as the Municipality of Kiryat Ata acts to change the Supreme Court's decision, in the estimation of Supergas's management, based on its legal counsel, the chances of Supergas being charged for betterment levy are lower than 50%. |

**Note 31 - Contingent liabilities (Cont.)**

| The parties | Amount of claim | Nature of claim | Prospects of claim |
|---|---|---|---|
| 4. Action in tort against Supergas | Action in tort in the sum of approx. NIS 35.5 million, which has been amended to a sum of approx. NIS 70 million. | In August 2015, an action in tort was filed against Supergas by Tamboard Gypsum Products Ltd. and Tambour Ltd. for damage caused to a factory by an alleged failure of the gas system. | Supergas has filed a statement of defense as well as a third party notice against Tamboard's insurer. In January 2017, the court granted a motion for amendment of the statement of claim, adding the plaintiff's subsidiary as an additional plaintiff and amending the amount of the claim setting it at NIS 70 million for court fee purposes. In June 2017, the insurer of the plaintiff filed a fourth party notice in the sum of NIS 2 million against Supergas and its insurer. Following the filing of supplementary opinions on the damage issue in the case, the parties agreed to defer the dispute to mediation.<br><br>In the estimation of Supergas's management, its exposure in the claim in question does not exceed its deductible under the insurance policy held thereby. Supergas's financial statements include a provision that reflects the cost of the deductible. |
| 5. Action in tort against Canit Hashalom and a former officer | Action in tort in the sum of NIS 55 million and, on the other hand, a pecuniary claim by Canit Hashalom in the sum of NIS 15 million. | In May 2017, Canit Hashalom filed a pecuniary claim in the sum of NIS 15 million with the Tel Aviv District Court, against the companies Winditaly Ltd. and Gualini S.p.A. (jointly: "**Gualini**"), in relation to the performance of a project in which Gualini served as subcontractors. Along with the filing of the claim, Canit Hashalom forfeited a bank guarantee in the sum of NIS 2.7 million.<br>Gualini filed a statement of defense in which they denied Canit Hashalom's claims and filed a countersuit in the sum of NIS 55 million against Canit Hashalom and an officer, in which countersuit they alleged failure to pay the full contractual consideration, damage to reputation and loss of future profit in Israel and unlawful forfeiture of a bank guarantee. | The parties have deferred to mediation. Canit Hashalom estimates, based on its legal counsel, that the countersuit's chances as pertains to damage to reputation and loss of future profit and to the forfeiture of the bank guarantee are lower than 50%. Due to the preliminary stage, it is too early to estimate the rest of Gualini's claims. However, it appears that Canit Hashalom has good arguments to defend against the countersuit. |

**Note 31 - Contingent liabilities (Cont.)**

**C.** Additional claims (mostly legal and in insignificant amounts) arising from the ordinary course of business have been submitted against the Group companies.

**D.** The Group recorded provisions against the claims in the sum of approx. NIS 11 million (December 31, 2017 – approx. NIS 4 million). In the estimation of the Company's management, based on its legal counsel (and in respect of the Granite Group companies, in reliance on the estimation of the managements of the Granite Group companies , based on their legal counsel), the provisions recorded to settle the results of the claims outlined above are fair.

## Note 32 - Management of financial risks

### A. General:

The Group is exposed to the following risks, which derive from the use of financial instruments:

- Credit risk.
- Liquidity risk.
- Market risk (including currency risk, interest risk and other price risks).

Information is provided in this Note in respect of the Group's exposure to each of the abovementioned risks, the Group's objectives, its policy and its processes in respect of the measurement and management of the risk. Additional, quantitative disclosure is provided throughout these Consolidated Financial Statements.

The comprehensive responsibility for establishing the framework for the management of the financial risks of the Company and its subsidiaries (except for the risk management of the Granite segment, the senior housing segment and Azrieli E-Commerce, which is carried out thereby) (the "**Company**") and for overseeing the same rests with the Company's management.

The Company has a Finance Committee, which is responsible, *inter alia*, for supervising and monitoring the management of the Company's financial risks, and also supervises Management as pertains to the implementation of its decisions.

The person in charge of financial risks management in the Company is Ms. Irit Sekler-Pilosof, the Company's CFO.

The Company's managers routinely examine the market risks in the fields of interest, the index and the exchange rates and act to reduce the economic exposure that is inherent in those risks, whilst taking cost-benefit considerations, such as changes in the composition of the long-term and short-term bank credit, into account.

### B. Credit risk:

Credit risk is the risk of a financial loss that would be caused to the Group if a customer or a counter party to a financial instrument does not meet its contractual commitments, and it derives primarily from the debts of customers and other receivables, from the long-term loans that have been extended and from investments in securities.

The Group has no significant credit risk from its customers in the retail centers and malls segment, the leasable office and other space segment and the income-producing property in the U.S. segment, since the Group collects its income in respect of rent and management fees in advance. Moreover, in most cases, as collateral for the rent, the tenants are required to prove personal guarantees from third parties and/or bank guarantees and/or deposits, to the Company's satisfaction.

The Group has no significant credit risk from its customers in the senior housing segment, since the Group collects a significant portion of the deposit required of the resident prior to his moving into the apartment.

The Group has credit risk in respect of credit card companies' balances deriving from the current clearing of customers' credit cards in the e-commerce segment. Azrieli E-Commerce routinely examines customers' credit assessments and makes specific doubtful debt provisions, which, in the opinion of Azrieli E-Commerce's management, correctly reflect the loss entailed by debts the collection of which is doubtful.

**Note 32 - Management of financial risks (Cont.)**

**B. Credit risk: (Cont.)**

The Group has a credit risk deriving from companies in the Granite Group. The income of the companies in the Granite Group derives primarily from sales in Israel to customers in the field of energy alternatives and from sales to customers in the water and wastewater segment.

The companies in the Granite Group have a procedure for the extension of credit to a customer, which includes guidelines in respect of what is to be done when a new customer is opened, the procedure includes, *inter alia*, a check on its financial position, a check on stability and control over the credit extended to the customer, which relies on past experience and external raisings, as well as, where possible, the receipt of collateral, such as: bank guarantees, personal guarantees, charges on land, motor vehicles, and debt notes.

Moreover, the procedure includes a hierarchy of authority for the approval of the maximum amount of a customer's credit, which starts with the credit manager and going up to the credit committee, which is headed by the Chief Executive Officer of each subsidiary. The procedure on authorities for the approval of credit is presented to the financial forum of the boards of directors of each of the subsidiaries for approval. The procedure determines and defines a framework of responsibility for the collection of the payment from customers and also the ways in which customers' balances that are in arrears are to be dealt with. The routine monitoring of the receipts from customers is conducted by the credit and collection departments and by the credit committees and management in each subsidiary.

The Companies in the Granite Group recognize provisions for doubtful debts, which reflect their evaluation made in respect of the loss that is contained in the debts whose collection is in doubt. This provision is made up of specific balances as well as a general component of the loss, which is determined for certain groups of similar customers, in respect of losses that have occurred, but which have not yet been identified.

**C. Liquidity risk:**

Liquidity risk finds expression in the non-ability to meet the Group's financial commitments when they are due for payment. The Group's approach to the management of its liquidity risk is to ensure, in so far as it is possible, that there is a sufficient level of liquidity to meet its commitments on time. The Group verifies the existence of sufficient levels of cash and/or credit lines in accordance with the expected needs for the payment of the operating expenses, including the amounts that are required to meet the financial liabilities; the aforesaid does not take into account the potential impact of extreme occurrences, which it is not reasonably possible to forecast.

The Group is of the opinion that at the time of need, financing entities will grant it the credit required thereby for the purposes of its business.

**D. Market risks:**

Market risk is the risk that changes in market prices, such as the exchange rates of foreign currencies, the CPI, interest rates, the prices of capital instruments and risks associated with the prices of goods, will have an impact on the Group's income or on the value of its holdings in financial instruments and on inventory balances.

The objective of the management of market risks is to manage and supervise the exposure to market risk within the framework of generally accepted parameters.

**Note 32 - Management of financial risks (Cont.)**

**D. Market risks: (Cont.)**

Currency risk

The Company's functional currency is the New Israeli Shekel (NIS).

The Group has loans in U.S. dollars, therefore its financial results are exposed to the risk of a change in the dollar exchange rate. Most of the Group's income in the income-producing property in the U.S. segment is stated in U.S. dollars, such that a rise in the exchange rate as aforesaid leads to an increase in income from rent and in the value of the property and reduces this risk.

Companies in the Granite Group are exposed to currency risk in respect of the purchase of raw materials, fixed assets and export sales, which are stated in currencies that are different from the functional currency. The currencies in which most of the transactions are stated which are not NIS are the Euro and the US Dollar (most of the purchases of oil distillates are linked to the US Dollar). The companies examine, on an ongoing basis, the assets and the financial liabilities stated in foreign currency in order to mitigate the risks deriving from the changes in the exchange rates.

Interest rates risk

The Group has short-term and long-term credit at variable interest rates. Accordingly, its financial results (financing income/expenses) are exposed to the risk of a change in the interest rates.

Index risks

The Group has loans and bonds that are index-linked, and therefore its financial results (financing income/expenses) are exposed to the risk of a change in the Index.

Most of the Group's income in the retail centers and malls segment and in the leasable office and other space segment are linked to the CPI, such that an increase in the Index, as aforesaid, will lead to an increase in the rent income and a reduction in this risk.
Furthermore, the index rise bears an impact on the calculation of the value of investment properties due to the increase in rent revenues.

The companies in the senior housing sector have exposure in respect of the effect of changes in the CPI on the deposits of the residents in the senior home, which are linked to the CPI.

Currency risk - cash

As of December 31, 2018, a small part of the cash is managed overseas in the dollar currency, and therefore the Company may be exposed to fluctuations in the currency exchange rates. In general, and other than as specified by the Company in the 2010 Prospectus, the Company takes no protective measures against such exposures.

In addition, the Company has a material holding in Bank Leumi’s shares that are traded in TASE. Changes in the rate of Bank Leumi’s share may affect the equity. The Company does hedge against such exposures (see also Note 2U).

Risks associated with the prices of goods

The inventory in Supergas is comprised primarily of oil distillates and accordingly it is exposed to changes in the prices of oil distillates. Supergas acts to reduce the quantity of inventory that is exposed and adjusts the quantities of the inventory of distillates in accordance with the sales forecasts.

## Note 33 - Financial instruments

### A. Credit risk:

#### (1) Exposure to credit risk

The book value of the financial assets represents the maximum credit exposure. The maximum exposure to credit risk, as of the date of the Statement of Financial Position, was as follows:

| | Book Value | |
|---|---|---|
| | As of December 31 | |
| | 2018 | 2017 |
| | NIS in millions | NIS in millions |
| **Financial assets at amortized cost:** | | |
| Short-term deposits and investments | 47 | 144 |
| Trade accounts receivable | 342 | 285 |
| Other receivables | 102 | 153 |
| Receivables for work in progress | 3 | 8 |
| Non-current loans | 127 | 141 |
| Restricted investments | 19 | 19 |
| Loans to associates | 100 | 85 |
| Receivables in respect of franchise arrangement | 51 | 55 |
| | 791 | 890 |

The maximum exposure to credit risk in respect of trade accounts receivable, other receivables, receivables for work in progress, long-term loans , as of the Report Date, by geographical region, is mainly local and the exposure overseas is negligible.

**Note 33 - Financial instruments (Cont.)**

**A. Credit risk (Cont.):**

**(2) The aging of debts and losses from impairment**

The following is the aging of the trade accounts receivable, other receivables, including derivative financial instruments, receivables for work in progress, long-term loans:

| | As of December 31, 2018 | | As of December 31, 2017 | |
|---|---|---|---|---|
| | Gross | Impairment | Gross | Impairment |
| | NIS in millions | NIS in millions | NIS in millions | NIS in millions |
| Not in arrears | 555 | - | 573 | 1 |
| 0–30 days in arrears | 2 | - | 2 | - |
| 31-120 days in arrears | 10 | - | 8 | 1 |
| 121 days to one year in arrears | 6 | 1 | 6 | 1 |
| More than one year in arrears | 18 | 16 | 11 | 10 |
| | 591 | 17 | 600 | 13 |

The movements in the provision for impairment in respect of trade receivables, other receivables and non-current loans during the year were as follows:

| | As of December 31 | |
|---|---|---|
| | 2018 | 2017 |
| | NIS in millions | NIS in millions |
| Balance as of January 1 | 13 | 11 |
| Recognized impairment loss | 6 | 3 |
| Doubtful debts that became bad debts | (2) | (1) |
| Balance as of December 31 | 17 | 13 |

Several times in each reporting period, the Group reviews the impairment and takes into account the period of the debt, the collateral that is available thereto, the financial of the debtors and the chances of legal proceedings against them.

**Note 33 - Financial instruments (Cont.)**

**B. Liquidity risk:**

Set forth below are the projected repayment dates of the financial liabilities, including an estimate of interest payments:

| | As of December 31, 2018 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | **Book value** | **Forecasted cash flow** | **2019** | **2020** | **2021** | **2022** | **2023 forth** | **No repayment date /upon demand** |
| | **NIS in millions** | **NIS in millions** | **NIS in millions** | **NIS in millions** | **NIS in millions** | **NIS in millions** | **NIS in millions** | **NIS in millions** |
| **Non-derivative financial liabilities** | | | | | | | | |
| Short-term credit from financial corporations (1) | 484 | 484 | 484 | - | - | - | - | - |
| Trade accounts payable | 342 | 342 | 342 | - | - | - | - | - |
| Other payables | 65 | 65 | 65 | - | - | - | - | - |
| Deposits from customers | 942 | 942 | - | - | - | - | - | 942 |
| Long-term loans from financial corporations (2) | 2,638 | 3,057 | 491 | 423 | 825 | 146 | 1,172 | - |
| Bonds (2) | 6,887 | 7,424 | 780 | 775 | 765 | 755 | 4,349 | - |
| Long-term deposits from customers | 59 | 59 | - | - | 56 | - | 3 | - |
| | 11,416 | 12,373 | 2,162 | 1,198 | 1,646 | 901 | 5,524 | 942 |

## Note 33 - Financial instruments (Cont.)

### B. Liquidity risk: (Cont.)

| | As of December 31, 2017 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Book value | Forecasted cash flow | 2018 | 2019 | 2020 | 2021 | 2022 forth | No repayment date /upon demand |
| | NIS in millions | NIS in millions | NIS in millions | NIS in millions | NIS in millions | NIS in millions | NIS in millions | NIS in millions |
| **Non-derivative financial liabilities** | | | | | | | | |
| Short-term credit from financial corporations (1) | 630 | 630 | 630 | - | - | - | - | - |
| Trade accounts payable | 296 | 296 | 296 | - | - | - | - | - |
| Other payables | 46 | 46 | 46 | - | - | - | - | - |
| Deposits from customers | 792 | 792 | - | - | - | - | - | 792 |
| Long-term loans from financial corporations (2) | 2,765 | 3,126 | 532 | 457 | 401 | 767 | 969 | - |
| Bonds (2) | 5,901 | 6,449 | 522 | 647 | 643 | 634 | 4,003 | - |
| Long-term deposits from customers | 48 | 48 | - | - | 48 | - | - | - |
| | 10,478 | 11,387 | 2,026 | 1,104 | 1,092 | 1,401 | 4,972 | 792 |

**(1)** The book value includes accrued interest.

**(2)** The book value includes current maturities and accrued interest.

**Note 33 - Financial instruments (Cont.)**

## C. Index and foreign currency risks:

### (1) Exposure to Index and foreign currency risk

The Group's exposure to Index and foreign currency risk, based on nominal values, is as follows:

| | As of December 31, 2018 | | |
|---|---|---|---|
| | Israeli currency | Foreign currency | |
| | Index-linked | Dollar | Other (*) |
| | NIS in millions | NIS in millions | NIS in millions |
| Assets | 105 | 221 | 5 |
| Liabilities | (9,009) | (1,509) | (22) |
| **Total net assets** | (8,904) | (1,288) | (17) |

(*) Mainly Euro and GBP.

| | As of December 31, 2017 | | |
|---|---|---|---|
| | Israeli currency | Foreign currency | |
| | Index-linked | Dollar | Other (*) |
| | NIS in millions | NIS in millions | NIS in millions |
| Assets | 98 | 201 | 4 |
| Liabilities | (8,025) | (1,221) | (23) |
| **Total net assets** | (7,927) | (1,020) | (19) |

(*) Mainly Euro and GBP.

**Note 33 - Financial instruments (Cont.)**

**C. Index and foreign currency risks: (Cont.)**

**(2) Sensitivity analysis**

The strengthening of the New Israeli Shekel against the following currencies as of December 31, 2018 and an increase in the CPI would increase (decrease) the capital and the profit or loss, net of tax, by the amounts that are presented below. This analysis has been made on the assumption that the other variables, and especially the interest rates, remain fixed. The analysis in respect of the year 2017 was made on the same basis.

| | As of December 31, 2018 | |
|---|---|---|
| | Capital | Profit (loss) |
| | NIS in millions | NIS in millions |
| 1% rise in the CPI | (69) | (69) |
| 3% rise in the exchange rate of the US Dollar | (30) | (30) |

| | As of December 31, 2017 | |
|---|---|---|
| | Capital | Profit (loss) |
| | NIS in millions | NIS in millions |
| 1% rise in the CPI | (60) | (60) |
| 3% rise in the exchange rate of the US Dollar | (23) | (23) |

A decrease in the exchange rate of the US Dollar by a similar rate and a decrease in the CPI by a similar rate as of December 31, 2018 would have had an identical effect, although in an opposite direction, in the same amount, assuming that all of the other variables remain constant.

**Note 33 - Financial instruments (Cont.)**

**D. Interest rate risk:**

**Type of interest**

Following are details in respect of the types of interest in the Group's interest bearing financial instruments:

| | Book value | |
|---|---|---|
| | As of December 31 | |
| | 2018 | 2017 |
| | NIS in millions | NIS in millions |
| **Fixed interest instruments** | | |
| Financial assets | 109 | 200 |
| Financial liabilities | 9,539 | 8,700 |
| **Variable interest instruments** | | |
| Financial assets | 119 | 141 |
| Financial liabilities | 509 | 664 |

**(1) Sensitivity analysis for the fair value in respect of fixed interest instruments**

The Group's assets and liabilities at fixed interest are not measured at fair value through profit and loss, therefore, a change in the interest rates as of the Report Date is not expected to have any impact on the profit or loss in respect of changes in the value of assets and liabilities with fixed interest rates.

**(2) Sensitivity analysis for variable interest instruments**

A change of 1% in the interest rates on the reporting date would increase or reduce the capital and the profit or loss, net of tax, by the sum of NIS 3 million. This analysis was made assuming that the other variables remained fixed.

**E. Other price risk:**

**Sensitivity analysis of the security price – financial assets at fair value through other comprehensive income – (see Note 11A)**

If the prices of the held securities were higher by 1%, the effect after tax would be as follows:

The net income for the year ending on December 31, 2018 would not be affected since these investments are accounted for through other comprehensive income.

The other comprehensive income would increase by approx. NIS 9 million as of December 31, 2018 as a result of the change in the fair value of the shares.

## Note 34 – Fair value

### A. Assets and liabilities measured at fair value in the Statement of Financial Position:

For the purpose of measurement of the fair value of the assets or liabilities, the Group classifies them in accordance with the rating that includes the following three levels:

**Level 1**: Quoted (not adjusted) prices in active markets for identical assets or identical liabilities to which the entity has access at the time of measurement.

**Level 2**: Data, other than quoted prices included in level 1, that are directly or indirectly observable for the asset or liability.

**Level 3**: Non-observable data for the asset or liability.

The classification of the assets or liabilities that are measured at fair value is based on the lowest level significantly used for measuring the fair value of the entire asset or liability.

Below are the Group's assets and liabilities measured at fair value in the Company's Statement of Financial Position as of December 31, according to their measurement levels.

**Fair value of items measured at fair value on a periodic basis**

| | As of December 31, 2018 | | |
|---|---|---|---|
| | Level 2 | Level 3 | Total |
| | NIS in millions | NIS in millions | NIS in millions |
| **Investment property:** | | | |
| Retail centers and malls in Israel | 49 | 11,820 | 11,869 |
| Land and leasable office and other space in Israel | 598 | 8,274 | 8,872 |
| Investment property under construction in Israel | - | 2,448 | 2,448 |
| Senior housing | - | 1,740 | 1,740 |
| **Total investment property in Israel** | 647 | 24,282 | 24,929 |
| Income-producing property in the U.S. | 374 | 2,149 | 2,523 |
| **Total investment property** | 1,021 | 26,431 | 27,452 |

| | As of December 31, 2017 | | |
|---|---|---|---|
| | Level 2 | Level 3 | Total |
| | NIS in millions | NIS in millions | NIS in millions |
| **Investment property:** | | | |
| Retail centers and malls in Israel | - | 11,842 | 11,842 |
| Land and leasable office and other space in Israel | 257 | 8,075 | 8,332 |
| Investment property under construction in Israel | - | 1,887 | 1,887 |
| Senior housing | - | 1,212 | 1,212 |
| **Total investment property in Israel** | 257 | 23,016 | 23,273 |
| Income-producing property in the U.S. | - | 1,933 | 1,933 |
| **Total investment property** | 257 | 24,949 | 25,206 |

**Note 34 – Fair value (Cont.)**

**A. Assets and liabilities measured at fair value in the Statement of Financial Position (Cont.)**

**Fair value of items measured at fair value on a periodic basis (Cont.)**

**Financial assets and liabilities:**

| | As of December 31, 2018 | | |
|---|---|---|---|
| | Level 1 | Level 2 | Total |
| | NIS in millions | NIS in millions | NIS in millions |
| **Financial assets designated at fair value through profit and loss:** | | | |
| Securities | 1 | - | 1 |
| Non-marketable investments | - | 10 | 10 |
| **Financial assets at fair value through other comprehensive income:** | | | |
| Marketable shares | 1,218 | - | 1,218 |
| Non-marketable shares – held for sale | - | 450 | 450 |
| **Total fair value of financial assets** | 1,219 | 460 | 1,679 |

| | As of December 31, 2017 | | | |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Total |
| | NIS in millions | NIS in millions | NIS in millions | NIS in millions |
| **Financial assets designated at fair value through profit and loss:** | | | | |
| Securities held for trade | 1 | - | - | 1 |
| Non-marketable investments | - | 17 | - | 17 |
| **Financial assets designated at fair value through profit and loss:** | | | | |
| Marketable shares | 1,132 | - | - | 1,132 |
| Non-marketable shares | - | 87 | 536 | 623 |
| **Total fair value of financial assets** | 1,133 | 104 | 536 | 1,773 |

**Note 34 – Fair value (Cont.)**

**B. Assets and liabilities measured at fair value at level 3 in the Statement of Financial Position:**

**(1) Movement in investment property measured at fair value**

| | Real estate in Israel | | | | Real estate in the U.S. | |
|---|---|---|---|---|---|---|
| | Retail centers and malls | Offices and other | Senior housing | Under construction | Income-producing property | Total |
| | NIS in millions | NIS in millions | NIS in millions | NIS in millions | NIS in millions | NIS in millions |
| **Balance as of January 1, 2018** | 11,842 | 8,075 | 1,212 | 1,887 | 1,933 | 24,949 |
| Profits or losses recognized: | | | | | | |
| in profit or loss | (30) | 147 | 89 | 78 | (45) | 239 |
| Purchases | 183 | 196 | 19 | 584 | 112 | 1,094 |
| Classifications | (175) | (144) | 420 | (101) | - | - |
| Dispositions | - | - | - | - | (5) | (5) |
| Net translation differences deriving from the translation of the financial statements of foreign operations | - | - | - | - | 154 | 154 |
| **Balance as of December 31, 2018** | 11,820 | 8,274 | 1,740 | 2,448 | 2,149 | 26,431 |

**Note 34 – Fair value (Cont.)**

**B. Assets and liabilities measured at fair value at level 3 in the Statement of Financial Position: (Cont.)**

**(1) Movement in investment property measured at fair value (Cont.)**

| | Real estate in Israel | | | | Real estate in the U.S. | |
|---|---|---|---|---|---|---|
| | Retail centers and malls | Offices and other | Senior housing | Under construction | Income-producing property | Total |
| | NIS in millions | NIS in millions | NIS in millions | NIS in millions | NIS in millions | NIS in millions |
| **Balance as of January 1, 2017** | 10,922 | 5,267 | 1,086 | 3,720 | 1,960 | 22,955 |
| Profits or losses recognized: | | | | | | |
| in profit or loss | (23) | 180 | 59 | 453 | (186) | 483 |
| Entry into consolidation(*) | - | - | - | - | 124 | 124 |
| Purchases | 174 | 36 | 17 | 732 | 67 | 1,026 |
| Classifications | 588 | 2,448 | - | (3,036) | - | - |
| Carried from level 2 | 181 | 144 | 50 | 36 | 174 | 585 |
| Carried to fixed assets | - | - | - | (18) | - | (18) |
| Net translation differences deriving from the translation of the financial statements of foreign operations | - | - | - | - | (206) | (206) |
| **Balance as of December 31, 2017** | 11,842 | 8,075 | 1,212 | 1,887 | 1,933 | 24,949 |

(*) See Note 13D(2).

**Note 34 – Fair value (Cont.)**

**B. Assets and liabilities measured at fair value at level 3 in the Statement of Financial Position (Cont.):**

**(2) Movement in assets and liabilities measured at fair value**

| | For the year ended December 31 | |
|---|---|---|
| | 2018 | 2017 |
| | NIS in millions | NIS in millions |
| **Financial assets at fair value through other comprehensive income:** | | |
| Balance as of beginning of year | 536 | 562 |
| Carried to assets held for sale | (450) | - |
| **Total losses recognized:** | | |
| In other comprehensive income | (86) | (26) |
| | - | 536 |

## Note 34 – Fair value (Cont.)

### B. Assets and liabilities measured at fair value at level 3 in the Statement of Financial Position (Cont.)

#### (3) Description of evaluation techniques

| Description of the measured instrument | Fair value as of December 31, 2018 | Evaluation technique | Description of significant non-observable data | Range | Other data | Range |
|---|---|---|---|---|---|---|
| | NIS in millions | | | | | |
| Retail centers and malls in Israel | 11,816 (2) | Income approach – discounted cash flows (DCF) | Primary cap rate | 6.75%-8% | Marketable space (in sqm in thousands) | 1-40 thousand sqm |
| | | | Fair value per sqm in NIS in thousands (3) | NIS 12-52 thousand | | |
| | | | Occupancy rate (**) (3) | 85%-100% | | |
| Land | 4 | Cost approach | | | | |
| **Offices and others in Israel:** | | | | | | |
| Existing office space for lease | 8,136 (2) | Income approach - discounted cash flows (DCF) | Primary cap rate (3) | 6.75%-8% | Marketable space (in sqm in thousands) | 2-151 thousand sqm |
| | | | Fair value per sqm in NIS in thousands | NIS 5-20 thousand | | |
| | | | Occupancy rate (**) (3) | 78%-100% | | |
| Other space for lease | 100 (2) | Income approach - discounted cash flows (DCF) | Estimated average rent per sqm in NIS (*) | NIS 28 | | |
| | | | Primary cap rate | 7.25% | | |
| Land | 38 | Comparison method | Size-specific adjustment | | | |

**Note 34 – Fair value (Cont.)**

**B. Assets and liabilities measured at fair value at level 3 in the Statement of Financial Position (Cont.)**

**(3) Description of evaluation techniques (Cont.)**

| Description of the measured instrument | Fair value as of December 31, 2018<br>NIS in millions | Evaluation technique | Description of significant non-observable data | Range | Other data | Range |
|---|---|---|---|---|---|---|
| Buildings under construction in Israel | 308 (2) | Discounted cash flows (DCF), net of the estimated construction costs expected to arise for completion thereof | Estimated rent per sqm in NIS | Retail NIS 130-260 | Estimated balance of construction costs expected per sqm marketable space | NIS 1,143-2,667 per sqm |
| | | | Primary cap rate | 8%-8.5% | | |
| | 2,001 | Comparison method | Specific adjustment for location, size and standard<br>Estimated betterment levy | | | |
| | 139 | Cost approach | | | | |
| Income-producing property in the U.S. | 2,131 | Income approach – discounted cash flows (DCF) | Estimated average rent per sqm in dollars (*) | $17-22 | Marketable space (in sqm in thousands) | 3-89 thousand sqm |
| | | | Primary cap rate | 5.75%-7.50% | | |
| | | | Fair value per sqm in NIS in thousands | 8-14 thousand sqm | | |
| | | | Occupancy rate (**) | 67%-100% | | |
| | 18 | Comparison method | Size and standard | | | |
| Senior housing | 1,684 (3) | Income approach – discounted cash flow (DCF) | Cap rate | 8.75% | | |
| | | | Annual resident turnover rate | 6.7%-10% | | |
| | 56 | Cost approach | | | | |

**Note 34 – Fair value (Cont.)**

**B. Assets and liabilities measured at fair value at level 3 in the Statement of Financial Position (Cont.)**

**(3) Description of evaluation techniques (Cont.)**

(*) Calculated on the basis of average rent per marketable meter in each property separately.

(**) Calculated on the basis of each property separately, excluding properties that are in stages of inhabitation.

(1) The fair value estimate will increase if the growth rate increases and/or the weighted cap rate decreases.

(2) The fair value estimate will increase if construction costs per sqm decrease, the rent payments increase, the weighted cap rate decreases and/or the value of the senior housing units increases.

(3) Including properties under inhabitation.

## Note 34 – Fair value (Cont.)

### B. Assets and liabilities measured at fair value at level 3 in the Statement of Financial Position (Cont.)

#### (3) Description of evaluation techniques (Cont.)

| Description of the measured instrument | Fair value as of December 31, 2017 | Evaluation technique | Description of significant non-observable data | Range | Other data | Range |
|---|---|---|---|---|---|---|
| | NIS in millions | | | | | |
| Financial assets available for sale | 536 (1) | Discounted cash flow | Weighted average cost of capital (WACC) | 8.5% | | |
| | | | Growth rate | 2.5% | | |
| Retail centers and malls in Israel | 11,657 (2) | Income approach – discounted cash flow (DCF) | Primary cap rate | 6.75% - 8% | Marketable space (in sqm in thousands) | 5-40 sqm in thousands |
| | | | Fair value per sqm in NIS in thousands (3) | NIS 12-52 thousand | | |
| | | | Occupancy rate (**) (3) | 90% - 100% | | |
| Land | 185 | Comparison method | Size-specific adjustment | | | |
| **Offices and others in Israel:** | | | | | | |
| Existing office space for lease | 7,798 (2) | Income approach - discounted cash flow (DCF) | Primary cap rate (3) | 6.75% - 8.5% | Marketable space (in sqm in thousands) | 2-151 sqm in thousands |
| | | | Fair value per sqm in NIS in thousands | NIS 6-17 thousand | | |
| | | | Occupancy rate (**) (3) | 83%-100% | | |
| Other space for lease | 95 (2) | Income approach - discounted cash flow (DCF) | Estimated average rent per sqm in NIS (*) | NIS 28 | | |
| | | | Primary cap rate | 7.50% | | |
| Land | 182 | Comparison method | Size-specific adjustment | | | |

**Note 34 – Fair value (Cont.)**

**B. Assets and liabilities measured at fair value at level 3 in the Statement of Financial Position (Cont.)**

**(3) Description of evaluation techniques (Cont.)**

| Description of the measured instrument | Fair value as of December 31, 2017 NIS in millions | Evaluation technique | Description of significant non-observable data | Range | Other data | Range |
|---|---|---|---|---|---|---|
| Buildings under construction in Israel | 269 (2) | Discounted cash flow (DCF), net of the estimated construction costs expected for the completion thereof | Estimated rent per sqm in NIS | Retail NIS 128-235 | Estimated balance of construction costs expected per sqm marketable space | 1,143-2,095 per sqm |
| | | | Primary cap rate | 8.5% | | |
| | 271(2) (4) | Discounted cash flow (DCF), net of the estimated construction costs expected for the completion thereof | Estimated tenant deposit against residential units | NIS 1.3-2.0 million | Estimated balance of construction costs expected per sqm building rights | NIS 4,000-4,286 per sqm |
| | | | Primary cap rate | 9.5% | | |
| | | | Annual tenant turnover rate | 10% | | |
| | 1,246 | Comparison method | Specific adjustment for location, size and standard<br>Estimated betterment levy | | | |
| | 101 | Cost approach | | | | |
| Income-producing property in the U.S. | 1,912 (2) | Income approach – discounted cash flow (DCF) | Estimated average rent per sqm in dollars (*) | $17-20 | Marketable space (in sqm in thousands) | 3-89 sqm in thousands |
| | | | Primary cap rate | 5.75% - 7.75% | | |
| | | | Fair value per sqm in NIS in thousands | NIS 6-13 thousand | | |
| | | | Occupancy rate (**) | 76%- 100% | | |
| | 21 | Comparison method | Size and standard | | | |
| Senior housing | 1,160 (2) | Income approach – discounted cash flow (DCF) | Cap rate | 8.75% | | |
| | | | Annual tenant turnover rate | 10% | | |
| | 52 | Cost approach | | | | |

**Note 34 – Fair value (Cont.)**

**B. Assets and liabilities measured at fair value at level 3 in the Statement of Financial Position (Cont.)**

**(3) Description of evaluation techniques (Cont.)**

(*) Calculated on the basis of average rent per marketable meter in each property separately.

(**) Calculated on the basis of each property separately.

(1) The fair value estimate will increase if the growth rate increases and/or the weighted cap rate decreases.

(2) The fair value estimate will increase if construction costs per sqm decrease, the rent payments increase, the weighted cap rate decreases and/or the value of the senior housing units increases. A 5% increase or decrease in the average rent per sqm, will increase or reduce the market value of the offices at Azrieli Center by approx. NIS 133 million, respectively. In addition, a 0.25% decrease or increase in the cap rate will increase their market value by approx. NIS 113 million or reduce the same by approx. NIS 105 million, respectively.

(3) Including properties under inhabitation.

(4) Relates to senior housing.

**Note 34 – Fair value (Cont.)**

**C.** For a description of the evaluation processes used in determining the fair value – see Note 3C.

**D. Fair value of items that are not measured at fair value in the Statement of Financial Position:**

**(1) Fair value by comparison to the book value**

Following are details regarding the fair value of certain items that are not measured at fair value in the Statement of Financial Position.

| | | As of December 31 | | | |
|---|---|---|---|---|---|
| | | 2018 | | 2017 | |
| | Level of fair value | Book value | Fair value | Book Value | Fair value |
| | | NIS in millions | NIS in millions | NIS in millions | NIS in millions |
| **Non-current assets:** | | | | | |
| Receivables in respect of franchise arrangement (1) | 2 | 51 | 66 | 55 | 74 |
| **Non-current liabilities:** | | | | | |
| Loans from banks and other credit providers (1) | 2 | 2,638 | 2,692 | 2,765 | 2,823 |
| Bonds (2)(1) | 1 | 6,887 | 6,940 | 5,901 | 6,170 |
| | | 9,525 | 9,632 | 8,666 | 8,993 |

(1) The book value includes current maturities and accrued interest.
(2) See Note 3C on the basis for the determination of the fair value.

**Note 34 – Fair value (Cont.)**

**D. Fair value of items that are not measured at fair value in the Statement of Financial Position: (Cont.)**

**(2) The interest rates used in the determination of the fair value**

The interest's rates used in the discounting of the expected cash flows, where relevant, are based on the government yield curve for each individual type of loan, as of the Report Date, with the addition of an appropriate fixed credit margin, as follows:

| | As of December 31 | |
|---|---|---|
| | 2018 | 2017 |
| | % | % |
| **Non-current assets:** | | |
| Receivables in respect of franchise arrangement | 1.91-2.48 | 1.11-1.88 |
| **Non-current liabilities:** | | |
| Loans from banks and other credit providers | 0.64-4.22 | 0.76 - 4.36 |
| Bonds | 0.64-1.59 | 0.62 - 0.92 |

**Note 35 – Related and interested parties**

**A. Parent company, controlling shareholder and subsidiary:**

As stated in Note 1A, the Company is held by Nadav Investments (the "**Parent Company**"), a company controlled by Ms. Sharon Azrieli, Naomi Azrieli and Danna Azrieli. On material subsidiaries, see Note 9 in respect of the Group's entities.

**B. Benefits for key managerial personnel (including directors who are employed by the Company):**

Benefits in respect of the employment of key management personnel (including directors who are employed in the Company) include:

| | For the year ended December 31 | | | | | |
|---|---|---|---|---|---|---|
| | 2018 | | 2017 | | 2016 | |
| | No. of persons | Amount | No. of persons | Amount | No. of persons | Amount |
| | | NIS in millions | | NIS in millions | | NIS in millions |
| Short-term benefits (1) (2) | 20 | 29.8 | 19 | 28.6 | 15 | 21.4 |
| Other long-term benefits | 2 | 1.8 | 2 | 0.3 | 2 | 0.5 |
| | | 31.6 | | 28.9 | | 21.9 |

(1) Also see Note 35C below.

(2) Including 8 directors who are not employed by the Company (in the years 2017 and 2016 – 8 directors and 7 directors, respectively).

**Note 35 – Related and interested parties (Cont.)**

**C. Transactions and balances with related and interested parties:**

| | For the year ended December 31 | | | As of December 31 | |
|---|---|---|---|---|---|
| | 2018 | 2017 | 2016 | 2018 | 2017 |
| | Amounts of transactions | | | Balance in balance sheet | |
| | NIS in millions | NIS in millions | NIS in millions | NIS in millions | NIS in millions |
| **Interested parties and affiliates owned by interested parties** | | | | | |
| Rent income | 1 | 1 | 1 | | |
| Donations (7) | 14 | 14 | .124 | | |
| Trade and other payables | | | | 0.1 | 0.2 |
| **Associates** | | | | | |
| Financing income | 4.6 | 4.6 | .58 | | |
| Loans and capital notes to associates | | | | 249.1 | 228.8 |

| | Amounts of Transactions | | |
|---|---|---|---|
| | For the year ended December 31 | | |
| | 2018 | 2017 | 2016 |
| | NIS in millions | | |
| **Key management personnel (including directors) in the Company (*)** | | | |
| Interested parties who are employed by the Company | .110 | 9.7 | 8.5 |
| Number of persons to whom the benefit relates | 2 | 2 | 2 |
| Director remuneration for interested parties who are not employed by the Company | 0.2 | 0.2 | 0.2 |
| Number of persons to whom the benefit relates | 2 | 2 | 2 |
| Remuneration for directors who are not employed by the Company (**) | 1.4 | 1.6 | 2.7 |
| Number of persons to whom the benefit relates | 6 | 6 | 6 |

(*) This information is included in Section B above.
(**) See Note 35C(9).

**Note 35 – Related and interested parties (Cont.)**

**C. Transactions and balances with related and interested parties: (Cont.)**

**(1)** On December 28, 2014, after receiving the approval of the Company's Compensation Committee and Board, the general meeting of the Company approved the engagement in a management agreement with Ms. Danna Azrieli with respect to the terms and conditions of her office and employment as Active Chairman of the Board of the Company, an agreement which took effect on January 1, 2015, and the principles of which are specified below:

The Management Services, as hereinafter defined, shall be provided to the Company by Ms. Danna Azrieli through a company wholly-owned by Ms. Danna Azrieli (the "**Management Company**"), in the framework of which services, Ms. Danna Azrieli shall serve as the Active Chairman of the Board of the Company on a full-time basis (100% position) (it is clarified that Ms. Danna Azrieli may continue to take additional actions, including philanthropic activities in which she is involved, from time to time, provided that the performance thereof does not affect the discharge of her duties in the Company) and shall provide the following services to the Company, through the Management Company: chairman of the executive board of the Company's management, overseeing the implementation of strategic decisions, formulating business and managerial decisions related to the development and management of the Company's properties, business development, financing and budget, targets and the examination of new operating segments, providing ongoing managerial and professional advice to the Company's management and the managers of the principal operating segments, overseeing, accompanying and analyzing business opportunities and leading transactions and acquisitions in Israel and overseas, overseeing existing projects and monitoring their progress, overseeing development and construction and business development abroad, responsibility for outlining the Company's community relations and representing the Company in conferences in Israel and abroad (the "**Management Services**").

In consideration for the provision of the Management Services, the Company shall pay Ms. Danna Azrieli (through the Management Company) the following consideration:

Fixed component – Annual management fee in the amount of approx. NIS 2.7 million (in nominal terms) (constituting, as of December 2014, monthly management fee of approx. NIS 225,000), plus V.A.T. as required by law, linked to the rise in the CPI for November 2014, which was published on December 15, 2014 (the "**Fixed Management Fee**") (in the event of a decline in the Index in a particular month, the consideration will not be reduced, but the reduction will be offset against future index rises). The Fixed Management Fee will be paid every current calendar month.

Variable component – for the Management Services, the Management Company shall be entitled to an annual bonus, for each calendar year, deriving from the Adjusted Profit, as specified below:

The “Adjusted Profit” for purposes of this section, for every calendar year – the annual pre-tax profit, according to the Company’s audited consolidated annual financial statements, net of the following amounts: (1) dividend received thereby from financial assets available for sale, which was included in the annual pre-tax profit; (2) profit (loss) deriving from the revaluation of real estate properties; (3) results of companies which do not engage in the Company’s core business segments (real estate) and were included in the annual pre-tax profit; (4) linkage differentials accrued on financial liabilities; (5) interest expenses, at the actual weighted effective interest rate for such year, of the Company and companies controlled thereby, which engage in the Company’s core business, on loans (regardless of whether or not they were taken) at a financing rate of 65% on the historical purchase cost in the books of the investment in companies which are not in the core business; (6) the sum total of the management fee (including bonus) to Ms. Danna Azrieli for such year, as included in the annual pre-tax profit; and (7) profit (loss) from financial assets (marketable securities) held for trading, including interest and dividend in respect thereof.

**Note 35 – Related and interested parties (Cont.)**

**C. Transactions and balances with related and interested parties: (Cont.)**

**(1) (Cont.)**

Bonus threshold and brackets – in a year in which the Adjusted Profit is less than NIS 925 million – there is no bonus entitlement. In a year in which the Adjusted Profit ranges between NIS 925 million and NIS 1,050 million – a bonus shall be paid at the rate of 0.5% of the difference between the bonus threshold and the actual Adjusted Profit; in a year in which the Adjusted Profit exceeds NIS 1,050 million – for the portion of the Adjusted Profit exceeding NIS 1,050 million – the amount paid shall be 0.75% of the amount in excess of NIS 1,050 million, plus 0.5% of the difference between NIS 925 million and NIS 1,050 million.

Bonus cap and payment for a partial year – the sum total of the annual bonus for any calendar year as aforesaid shall not exceed NIS 1.5 million. If the Management Services shall have been rendered during part of a calendar year, the Management Company shall be entitled to a bonus calculated according to the relative part in the annual calculation results, on the basis of a 365 day year, in accordance with the part of the year during which the Management Services were rendered and based on the consolidated annual statements for such year in which the Management Agreement commenced or ended.

Clawback clause – if and insofar as it transpires *post factum* that the figures on which the Company relied when granting the annual bonus as aforesaid to Ms. Danna Azrieli are incorrect and that restatement thereof in the Company’s Financial Statements is required, Ms. Danna Azrieli shall repay the Company the difference between the amount of the bonus paid to her based on such incorrect figures and the amount of the annual bonus to which she is entitled based on the figures following such restatement.

Reimbursement of expenses, car and telecommunication – the Company shall bear all of the expenses of the Management Company in the context of the provision of the Management Services, including entertaining expenses, travel and *per diem* expenses in Israel and abroad, all in accordance with the Company's procedures and against presentation of appropriate evidence up to a maximum amount as shall be determined by the Company's Board from time to time and which shall be determined appropriate thereby, taking into account the Company's business and the scope thereof. The Company shall further bear the costs of making available and maintaining a car for the purpose of providing the Management Services, the costs of use of telephony and telecommunication, and may also, from time to time and in accordance with the compensation policy, grant Ms. Danna Azrieli additional related benefits, such as a laptop, internet connection, subscriptions to financial newspapers and daily newspapers, payment for participation in professional conferences, professional literature, seminars, etc. Reimbursement of car and telecommunication expenses shall not exceed a maximum amount as shall be determined from time to time by the Audit Committee and which shall be determined appropriate thereby, considering the Company's business and the scope thereof.

The agreement also includes the Company’s undertaking of inclusion within an officers’ insurance policy, and the grant of letters of exemption and indemnification in the standard language granted to the other officers of the Company, all subject to the provisions of the Companies Law and the approvals required thereunder, the Company's articles of association and the Company's compensation policy.

Term of the agreement and termination thereof – the management agreement took effect on January 1, 2015 for a three-year period as of such date, unless extended prior thereto by agreement between the parties and subject to receipt of all of the approvals required under law. The management agreement may be terminated by the Management Company, on the one hand, and by the Company, by way of a board resolution, on the other hand, subject to a prior notice of 6 months in advance (with no adjustment period), other than in exceptional events in which it may be terminated by the Company with immediate effect.

**Note 35 – Related and interested parties (Cont.)**

**C. Transactions and balances with related and interested parties: (Cont.)**

**(1) (Cont.)**

On October 6, 2016, the general meeting of the Company's shareholders approved the extension of the management agreement with Ms. Danna Azrieli, for a three-year period, from the aforesaid meeting approval date, with no change to the effective agreement as of such time.

The total management fee for 2018 totaled approx. NIS 4.2 million (in 2017 – approx. NIS 4.4 million).

**(2) Granite's general meeting has approved:**

**(a)** The provision of an indemnification in advance to all of the officers who are so entitled in Granite and in its consolidated companies, including officers who are considered to be controlling interests, in the past, present and future. The commitment to indemnification is limited to certain types of events and to amounts as detailed in the decision that was passed. The indemnification is in respect of the period in which Granite was a public company (until September 2012) and in connection with the office of the officers at such time.

The cumulative maximum amount of the indemnification, for all of the officers, may not exceed 20% of Granite's equity in accordance with the last financial statements that are known at the time of the passing of the decision in respect of the indemnification, with the addition of amounts that will be received from the insurance company.

**(b)** The granting of an exemption in advance to all of the officers who are so entitled in Granite and in its consolidated companies, including officers who are considered to be controlling interests, from liability in respect of damage caused as the result of a breach of the duty of care vis-à-vis the Company.

**(c)** Directors and officers liability insurance in Granite and in its subsidiaries, for a period of 12 months from November 1, 2018 and with limits of overall liability per case and for a period of U.S. $30 million.

**(d)** Expansion of the indemnification granted to Granite's directors and officers was approved such that it will apply also to events arising from the Improvement of Enforcement Law, within the limits of the law. Granite further limited the retroactive indemnification amount to 20% of its equity according to the Financial Statements, as being on the date of actual granting of the indemnification. Further approved was the granting of indemnification also to Ms. Danna Azrieli, who is deemed a controlling shareholder of the Company. The granting of the exemption to Ms. Danna Azrieli is subject to approval by the general meeting of Granite's shareholders.

**(3)** With respect to the guarantees that the Group has made available to companies in the Group, see Note 30B.

**Note 35 – Related and interested parties (Cont.)**

**C. Transactions and balances with related and interested parties: (Cont.)**

**(4)** On March 18, 2015, the Company’s Board approved, after the Audit Committee’s approval, for the sake of caution only, engagement in an agreement to receive consulting services from a company wholly owned and fully controlled by Mr. Menachem Einan (the “**Management Company**”) (the “**Consulting Agreement**”). According to the Consulting Agreement, the Management Company will provide consulting services on various strategic matters according to the Company’s requirement and up to a scope of 40 monthly hours, in consideration for monthly consulting fees of approx. NIS 60 thousand, linked to the Index, plus reimbursement of reasonable expenses. In addition, it was determined that insofar as the process of disposition of Sonol Israel Ltd. and/or Supergas Israel Gas Co. Ltd., from Granite Hacarmel Investments Ltd. group, which is controlled by the Company, is completed, the Management Company will be entitled to a one-time bonus of NIS 500 thousand in respect of each one of the dispositions, in accordance with the date set forth in the agreement.

The agreement is for a period of 24 months from March 1, 2015 (the “**Term of the Agreement**”), while each party is entitled to terminate the Consulting Agreement at any time after a period of 12 months from the date of its taking effect, in which case, the Company will continue to pay the Management Company monthly consulting fees for the entire remainder of the Term of the Agreement (all unless the agreement is breached). In the framework of the agreement, the Management Company committed to confidentiality and non-competition. On February 28, 2017 this agreement ended.

In 2016 Mr. Einan received a bonus in the amount of NIS 400 thousand, in accordance with the agreement between the parties, following the disposition of Sonol Israel Ltd.

Since March 2016, Mr. Einan serves as a director of the Company. In August 2016, the Company’s general meeting approved his appointment as a director.

In accordance with the resolutions of the Company’s Compensation Committee and Board, which were adopted on March 19 & 21, 2016 (respectively), since March 1, 2017, Mr. Einan receives director compensation in accordance with the Companies Regulations (Rules on External Directors’ Remuneration and Expenses), 5760-2000.

**(5)** On April 2, 2013, the Company's Board approved the appointment of Mr. Yuval Bronstein ("**Mr. Bronstein**") as the Company's CEO as of May 1, 2013, in lieu of his office as the Company’s CFO.

On June 20, 2013, the general meeting approved the terms of the Company's engagement in an agreement with a Company wholly-owned by Mr. Bronstein (the "**Management Company of Mr. Bronstein**").

The Management Company of Mr. Bronstein was entitled to a fixed monthly payment of NIS 255,000, linked to the rate of increase of the CPI for February 2013, as published on March 15, 2013, and to related benefits, including the provision of a vehicle (Group 7) and a mobile phone.

Each of the parties to the agreement may have terminated the agreement, for any reason whatsoever, by a prior written notice of three months.

Furthermore, the Management Company of Mr. Bronstein was entitled to adjustment compensation in an amount equal to 9 monthly payments.

On October 6, 2016, the general meeting of the Company’s shareholders approved an update to the management agreement with Mr. Bronstein, which updated the monthly management fees that were paid to the Management Company of Mr. Bronstein to the sum of NIS 313 thousand, linked to the June 2016 index. The remaining terms and conditions of Mr. Bronstein's engagement remain unchanged.
In 2017, Mr. Bronstein received a bonus in the sum of NIS 941 thousand (2016 – NIS 941 thousand).
In October 2017, Mr. Yuval Bronstein gave notice of the termination of his office on December 31, 2017.

**Note 35 – Related and interested parties (Cont.)**

**C. Transactions and balances with related and interested parties: (Cont.)**

**(6)** On October 19, 2017, the Board appointed Mr. Eyal Henkin ("**Mr. Henkin**") as the Company's CEO, as of January 1, 2018.

On April 30, 2018, the general meeting of the Company's shareholders approved the terms and conditions of Mr. Eyal Henkin's office and employment (through a private company wholly-owned by him) as CEO of the Company.

Mr. Henkin's management company is entitled to a fixed monthly payment of NIS 313 thousand, linked to the June 2016 index, as published in July 2016, and related benefits, including the provision of a vehicle (Group 7) and a mobile phone.

Each of the parties may terminate the agreement, for any reason whatsoever, by a prior written notice of three months.

Furthermore, Mr. Henkin's management company shall be entitled to an adjustment bonus in an amount equal to 9 monthly payments. In 2018, Mr. Henkin received a bonus in the sum of NIS 954 thousand.

**(7)**

**a.** On May 5, 2010, shortly before the Company's IPO, the Company's general meeting, after the approval of the Company's Board had been received on May 5, 2010, gave its approval that within the framework of the annual contributions which are given to NPO's by the Company, whose scope shall be determined by the Company's Board from time to time, the Company shall remit, *inter alia*, through contributions to the Azrieli Foundation (Israel) (R.A.), ("**AFI**"). The resolution was adopted based on an examination of the main objectives of AFI which are to act to promote education and culture in Israel, through projects in the field of education, culture, welfare and science, the execution of project and the conducting of research alone and/or in conjunction with other organizations, including by means of awarding grants to organizations and/or individuals for the purpose of the performance of projects and/or research work that accords with the objectives of the Foundation, which have been examined and found to accord with the Company's policy on contributions. There is nothing in the said decision that prevents the Company's Board from resolving to contribute to other charitable entities, whose objectives accord with the Company's policy on contributions, as they may be from time to time.

Within the framework of the said decision by the general meeting, it was determined that during the period until May 2015, the company will donate to the Foundation, in each calendar year, by itself or by means of companies that it controls (except for Granite), an amount that constitutes 1.5% of the Company's annual profit and in any event not more than an amount of NIS 14 million.

The contributions remitted by the Company to AFI were used for the making of donations and for the current needs of the AFI. This contribution is deemed as a contribution out of the Company's annual contribution budget, as determined by the Company's Board from time to time.

**Note 35 – Related and interested parties (Cont.)**

**C. Transactions and balances with related and interested parties: (Cont.)**

**(7) (Cont.)**

The Company's internal auditor was appointed by the Company's Board, to examine in each calendar year and prior to the time of the signing of the financial statements for that year, the total scope of the contributions that AFI has contributed in that year, and the correlation between the contribution that stood at the basis of the decision by the general meeting that approved the annual contribution, as aforesaid and shall submit a written report to the Audit Committee. In view of Amendment 16 to the Companies Law that shortened the transaction to 3 years, on March 14, 2013, the Company's Audit Committee approved the reasonableness of the period which was set at 5 years (namely – May 2015).

In May 2015, the general meeting (after the approval of the Audit Committee and the Company's Board) approved the Company's engagement with AFI in a new contribution arrangement, which extended the arrangement for contribution to AFI by another five years commencing on June 1, 2015 and ending on May 31, 2020.

**b.** On March 13, 2014, a contribution agreement (the "**Contribution Agreement**") was signed between Azrieli Holdings and the Azrieli Foundation (Israel) (R.A.) ( "**AFI**"), a non-profit association registered in Israel, which works, *inter alia*, to promote education and culture through projects in the fields of culture, welfare and science.

According to the terms of the Contribution Agreement, Azrieli Holdings granted AFI, by way of a contribution, for no consideration, 6,902,000 ordinary shares of par value NIS 0.1 each of the Company (the "**Contribution Shares**"), which constitute approx. 5.69% of the Company's issued capital.

According to the provisions of the Contribution Agreement, the contribution of the Contribution Shares to AFI was made subject to the following 3 conditions:

**(a)** AFI shall hold the Contribution Shares, shall not transfer the same nor make any other disposition therein, for a period of at least 10 years from the date of execution of the contribution agreement (the "**Limitation Period**"); upon expiration of the Limitation Period, any transfer of the Contribution Shares by AFI will require a resolution by a special majority of at least 75% of the members of the board (or any other required organ), who are entitled to participate in a vote on such resolution ("**Special Approval**");

**(b)** Upon expiration of the Limitation Period and subject to receipt of the Special Approval as aforesaid, any future transfer of the Contribution Shares will be subject to a right of first refusal in favor of Azrieli Holdings;

**(c)** Azrieli Holdings shall retain all of the voting rights under the Contribution Shares, to which end AFI has signed the necessary powers of attorney. In the case of a future sale of the Contribution Shares by AFI, the voting rights under the Contribution Shares shall pass to the buyer.

As a result of receipt of the Contribution Shares, AFI became an interested party, as this term is defined in the Securities Law, 5728-1968 (the "**Securities Law**"), in the Company. Pursuant to the provisions of the Contribution Agreement, Azrieli Holdings and AFI are considered "Joint Holders" within the definition thereof in the Securities Law. In the matter of duties applying or relating, according to the Companies Law, to controlling shareholders of a company, the Company chose to relate to AFI as if it is the controlling shareholder of the Company, even if this is not required according the provisions of the law, so long as the Company did not give another reporting.

**Note 35 – Related and interested parties (Cont.)**

**C. Transactions and balances with related and interested parties: (Cont.)**

**(7) (Cont.)**

**c.** On March 24, 2014, Azrieli Holdings transferred to The Azrieli Foundation, a registered Canadian philanthropic foundation whose assets are designated for donations and to fund philanthropic activity in Israel and in Canada (the "**Azrieli Foundation Canada**"), 460,000 shares of the Company as a contribution for no consideration, constituting approx. 0.38% of the Company's issued capital. After the transfer of the Company's shares, the Azrieli Foundation Canada held 13.68% of the Company's share capital.

In 2015 and 2016, Azrieli Foundation Canada sold some of the Company's shares that were held thereby, and after the sale of the shares and as of the Report Date, Azrieli Foundation Canada holds 8.55% of the Company's share capital.

**(8)** In November 2014, Gemel Tesua Investments Ltd. ("**Gemel Tesua**") entered into an agreement with Azrieli Foundation (Israel) R.A. ("**AFI**") (see Section 7 above), according to which Gemel Tesua will lease to AFI, under market conditions, from January 2015, an area of approx. 457 sqm out of the office space in the Herzliya Business Park project, which is owned by the Group, and will also provide AFI with management and maintenance services as it provides to the other tenants in the project, which include, *inter alia*, cleaning, maintenance, building insurance and third party insurance for the public areas, payments of municipal taxes in respect of the public areas and gardening, for a period of five years, with an option to extend the period for an additional five years, in consideration for a monthly payment of approx. NIS 58 thousand.

It was further agreed that Gemel Tesua will receive one-time compensation from AFI in respect of the investment budget provided in relation to the old area in the sum of NIS 313 thousand, linked to the index according to the previous agreement of 2010.

In October 2013, Gemel Tesua entered into an agreement with Candan Residences Ltd. ("**Candan Residences**"), a company controlled by the controlling shareholder and chairman of the Board, Ms. Danna Azrieli, whereby Gemel Tesua will lease to Candan Residences, at arm's length conditions, effective from October 2013, an area of approx. 190 sqm of the office space in the Herzliya Business Park project that is owned by the Group, and will provide to Candan Residences management and maintenance services as it does to the other tenants in the project which include, *inter alia*, cleaning, maintenance, building insurance, third party insurance for public areas, payment of municipal taxes for public areas and gardening, for a two-year period with an option to extend the period by two more years until October 14, 2017, in consideration for a monthly payment of approx. NIS 22 thousand. In October 2017 the agreement was extended with the same terms and conditions by two more years until October 14, 2019.

The Company classified the transactions as negligible transactions, under market conditions and in the ordinary course of business, and determined that they are not transactions which require special approvals pursuant to the Companies Law (the classification was made in relation to each transaction separately).

**(9)** Remuneration of the directors - in accordance with the decision of the Company's Board and the Company's general meeting, from May 10, 2010 and August 24, 2010, the remuneration of the external directors, who are appointed in the Company, to be in accordance with the Companies Regulations (Rules on External Directors' Remuneration and Expenses), 5760-2000 (the "**Remuneration**"). The annual remuneration and the remuneration for participation (including remuneration as an expert outside director) will be paid in accordance with the maximum amount that is set in the remuneration regulation, in accordance with the Company's capital grade, as it may be from time to time.

**Note 35 - Related and interested parties (Cont.)**

**C. Transactions and balances with related and interested parties: (Cont.)**

**(9) (Cont.)**

In accordance with the decision of the Company's Board and general meeting as of May 6, 2010, the payment to the Company's directors, except for the independent external directors and except for directors who receive fees from the Company (whether themselves or by means of management companies that they control), in an amount of NIS 65 thousand and remuneration for participation in meetings in an amount of NIS 2,300. The amounts of the Remuneration will be index-linked in accordance with the provisions of the Remuneration Regulations, In addition, the provisions of Sections 5 (B) and 6 (A) of the Remuneration Regulations will apply to the Remuneration paid to the directors, *mutatis mutandis*.

On May 13, 2013, following Amendment 16 to the Companies Law, after the approval of the Company's Compensation Committee had been received, the Company's Board approved the continued payment of the annual remuneration and the said participation remuneration to Naomi Azrieli and Sharon Azrieli under the same terms and conditions as specified above. On May 24, 2016, the Company's Board, following receipt of the approval of the Company's Audit Committee in its capacity as the Compensation Committee of May 22, 2016, approved the continuation of the payment of the annual compensation and participation compensation as aforesaid to Naomi Azrieli and Sharon Azrieli under the same terms and conditions as specified above. The approval of the compensation as aforesaid is for a three-year period, effective from June 3, 2016.

Such approvals were reported to the public in accordance with Regulation 1B(3) of the Companies Regulations (Relief in Transactions with Interested Parties), 5760-2000.

**D. Exemption, insurance and indemnification for officers and directors:**

**(1) Exemption:**

In accordance with the decision passed by the Board and the Company's shareholders meeting on May 6, 2010, the Company has granted officers and the directors, as they may be from time to time, with the exception of the indirect controlling shareholder directors, Sharon Azrieli, Naomi Azrieli and Danna Azrieli, an exemption in advance and retrospectively from their responsibility, in whole or in part, as a result of any damage that may be caused to it and/or that has been caused to it, whether directly or indirectly, as a result of a breach of a duty of care of the directors and the officers to it and to its subsidiaries, and as officers and/or as directors in the Company or officers and/or directors acting on the Company's behalf in the subsidiaries. For details regarding an amendment to the Company's articles with respect to the exemption, see Note 35D(3).

**Note 35 – Related and interested parties (Cont.)**

**D. Exemption, insurance and indemnification for officers and directors: (Cont.)**

**(2) Indemnification:**

On May 6, 2010, the Company's Board and general meeting approved the grant of indemnification to all of the officers in the Company and the directors of the Company, as being from time to time, for any liability or expenses as specified below, imposed thereon as a result of actions made (including actions made prior to the grant of letter of indemnification) and/or will make in their capacity as officers and/or directors of the Company and/or as officers and/or directors acting on the Company's behalf in the subsidiaries or affiliates of the Company or any other company in which the Company has an interest: (a) a financial indebtedness that is placed on an officer and/or director in favor of another person under a judgment, including a judgment issued by way of compromise or an arbitration award that is approved by a court and solely that those actions relate to one or more of the events that are detailed in the letter of indemnification; (b) reasonable litigation expenses, including lawyers' fees, which are expended by an officer and/or a director or that they were charged to pay by a court, in proceedings that were presented against them by the Company or in its name or in the name of another person, or on a criminal indictment that they are acquitted of, or on a criminal indictment on which they are found guilty and which does not require proof of criminal intent; (c) reasonable litigation expenses, including lawyers' fees that have been expended by an officer and/or a director, as the result of an investigation or proceedings that are conducted against them by an authority that is authorized to conduct the investigation or proceedings, and which ended without the presentation of an indictment against them and without any financial liability being placed upon them as an alternative to criminal proceedings, or which ended without the presentation of an indictment against them but with the placement of a financial liability as an alternative to criminal proceedings in a transgression which does not require proof of criminal intent.

The amount of the indemnification that the Company will pay to each officer (including directors), cumulatively in accordance with each letter of indemnification that is issued to them by the Company in accordance with the indemnification decision, in respect of one or more of the events that are detailed in the letter of indemnification, may not exceed 20% of the capital that is attributed to the shareholders in the Company in accordance with the last financial statements of the Company (audited or reviewed), which were published before the date of the indemnification.

After receipt of the approval of the Company's Board and the Audit Committee dated June 28, 2011, the general meeting approved the amendment to the language of the letters of exemption and indemnification which the Company granted and grants to the Company's officers and directors, including officers and directors of the Company who are deemed controlling shareholders and/or in the granting of which the controlling shareholders of the Company have a personal interest, as shall hold office from time to time, in order to adjust the same to the provisions of Section 56H of the Securities Law, such that they shall include an indemnification undertaking with respect to payments to persons injured by a breach and expenses in connection with administrative enforcement proceedings, including reasonable litigation expenses.

On December 28, 2014, after receipt of approval from the Company's Compensation Committee and Board, the Company's general meeting approved the extension of the letters of indemnification to the directors who are indirect controlling shareholders of the Company (Mmes. Danna, Sharon and Naomi Azrieli) for an additional three-year term from August 15, 2014, with no change in the terms and conditions of the letter of indemnification (whose language is identical to that to which the other directors are entitled as described in the Note), with the exception of the exemption component, which was not included in the letter of indemnification whose extension was approved as aforesaid.

**Note 35 – Related and interested parties (Cont.)**

**D. Exemption, insurance and indemnification for officers and directors: (Cont.)**

**(2) (Cont.)**

On August 9, 2016, the general meeting of the Company's shareholders approved amendments to the Company's articles, concerning mainly updates in accordance with legislative provisions that have changed, expansion of the liabilities and/or expenses for which the Company will be entitled to grant indemnification and/or insurance to directors and officers, *inter alia*, pursuant to the Restrictive Trade Practices Law, 5748-1988, and expansion of the term "Party Injured by a Breach" such that the this definition will apply to any and all acts of legislation pursuant to which an administrative proceeding may be held.

On October 6, 2016, the general meeting of the Company's shareholders approved an amendment to the exemption clause in the Company's articles such that following the amendment to the articles the Company may exempt, in advance and retrospectively, an officer thereof, of his liability, in whole or in part, for damage pursuant to a breach of the duty of care towards it, to the maximum extent permissible under any law, subject to the exemption not applying to a resolution or transaction in which the controlling shareholder or an officer of the Company have a personal interest.

On April 27, 2017, the general meeting of the Company's shareholders approved an amendment to and extension of letters of indemnification that had been granted to Ms. Danna Azrieli, Ms. Sharon Azrieli and Ms. Naomi Azrieli, the indirect controlling shareholders of the Company ("**Directors who are Controlling Shareholders**"), for an additional three-year period, and the grant of an exemption from liability to the Directors who are Controlling Shareholders for a three-year period, as of April 27, 2017.

On April 27, 2017, the general meeting of the Company's shareholders approved the grant of updated letters of indemnification and exemption to directors of the Company, as serving thereat from time to time, with the exception of directors who are controlling shareholders of the Company and/or their relatives.

**(3) Insurance:**

On May 24, 2016, the Company's Board approved (after the Compensation Committee's approval of the same date) engagement for renewal of the Company's insurance policy for directors and officers (including from among the Company's controlling shareholders) of the Company and the Company's subsidiaries, except in relation to the Granite Hacarmel group which holds an independent D&O insurance policy in accordance with the Company's compensation policy (as being at such time). On May 30, 2018, the Compensation Committee approved an engagement for the renewal of the D&O insurance policy of the Company (including from among the Company's controlling shareholders) and subsidiaries of the Company (except with respect to Granite Hacarmel, which holds an independent D&O insurance policy), from June 2018 until June 2019 (the "**Engagement**"). The Engagement is consistent with the engagement framework specified in the Company's approved compensation policy, and as specified below:

**1)** The limits of liability in the insurance policy shall not exceed U.S. $100 million per event and for the period of the insurance, plus reasonable legal defense costs in Israel, over and above the limits of liability, and in respect of claims filed outside of Israel – reasonable legal defense costs over and above the limits of liability, in accordance with trial costs customary in Israel and pursuant to the Israeli law.

**2)** The deductible per claim for the Company alone shall not exceed U.S. $150 thousand, in accordance with the cause of action and the place of filing thereof, and at an annual premium which has been and/or shall be paid which shall not exceed U.S. $250 thousand.

**Note 35 – Related and interested parties (Cont.)**

**D. Exemption, insurance and indemnification for officers and directors: (Cont.)**

**3)** The insurance policy was extended to cover claims that are filed against the Company (as distinguished from claims against directors and/or officers thereof), which concern the violation of securities law at least in Israel (entity coverage for securities claims), and procedures for the payment of insurance benefits shall be determined, whereby the right of the directors and/or officers to receive indemnification from the insurer pursuant to the policy shall precede the right of the Company.

**4)** The policy covers also the liability of the controlling shareholders in their capacity as directors and/or officers of the Company, and the terms of the coverage with respect thereto do not exceed those of the other directors and/or officers of the Company.

POSI type policy – On June 3, 2010 the Company purchased a POSI (Public Offering of Securities Insurance) type insurance policy, which covers the responsibility of the Company, the directors and the officers in it, the controlling interests and additional parties, who have taken part in public offering of the Company's shares in accordance with the prospectus that was issued in May 2010 (the "**Offering**"), against claims that may be filed against them in connection with the Offering and this for a period of 7 years from the time of the Offering. The maximum limits of liability of the insurer in accordance with this policy will not exceed U.S. $100 million per event and for the period of the insurance, plus reasonable legal defense costs over and above the limits of liability pursuant to the Israeli law. The annual premium is U.S. $250 thousand. The deductible per claim for the Company in respect of claims under this policy will not exceed U.S. $35 thousand.

**E. Negligible transactions:**

On November 24, 2010, the Company's Board decided to adopt guidelines and rules regarding the classification of transactions which are not irregular transactions, of the Company or of a consolidated company thereof with interested parties therein or controlling shareholders, as a negligible transactions. Such guidelines were prescribed, *inter alia*, considering the scope of the Company's assets, the diversity of its businesses, the nature of the transactions performed thereby and the level of effect thereof on the Company's business and results. In May 2015, the Company's Board adopted a master procedure for transactions with related parties, which consolidated and incorporated procedures that were approved at the Company in the years preceding the approval thereof, including in respect of classification of negligible transactions.

Such rules and guidelines will serve on the one hand for examining the need to approve the transaction at the relevant institutions in the Company, and on the other hand, for examining the duty and/or scope of disclosure in the periodic report and the prospectus (including in shelf offer reports), and/or the provision of an immediate report in respect of such a transaction. It is noted that the transactions are examined at the group level, including material companies controlled by the Company.

The Company's Board determined that a negligible transaction at the Company is a transaction of the Company with controlling shareholders or another person in which the controlling shareholder has a personal interest, which is not irregular (i.e. is in the ordinary course of business, under market conditions and not material), and meets the following tests:

**(1)** In respect of the duty to provide an immediate report in connection with a negligible transaction – a single transaction in a company or a subsidiary controlled thereby is a negligible transaction if the financial scope thereof does not exceed the rate of 0.1% of the Company's consolidated equity according to the last financial statements; in case of ongoing transactions (including rent, leases and so forth), according to the monthly transaction amount, or the total sum of the transaction for the whole duration of the engagement, according to the shorter/lower between them. For the purpose of immediate report, the negligibility of a transaction will be examined on the basis of the specific single transaction, and to the extent such will pass the negligibility threshold, the Company will report such transaction through an immediate report.

## Note 35 – Related and interested parties (Cont.)

### E. Negligible transactions: (Cont.)

**(2)** In respect of providing specification in the annual report in connection with negligible transactions – the total sum of all of the transactions of a certain type in the Company or a subsidiary controlled thereby, in a calendar year has not exceeded a rate of 0.5% of the Company’s consolidated equity according to the last annual reports. The Company will include the types of transactions and aggregate amount thereof within its annual report only if the total amount exceeds the rate stated above. For the purpose of reporting within a periodic report, financial statements and a prospectus (including a shelf proposition report), the negligibility of the aggregate of all of the transactions of the same type of the Company with the controlling shareholder or with corporations controlled by the controlling shareholder, will be examined on an annual basis.

**(3)** Integrated transactions - upon the classification of transactions as negligible or non-negligible, each transaction will be examined in itself, however, the negligibility of integrated transactions, or such that are contingent upon each other or transactions of the same type, will be examined in the aggregate as one transaction. In respect of multiannual transactions (agreements for a period of several years), the scope of transaction will be calculated for examination of the negligibility threshold on an annual basis (i.e. – the total monetary amount deriving from the transaction exceeding the negligibility threshold as aforesaid). In insurance transactions, the premium will be examined as the transaction amount. Regardless of the insurance coverage provided, multiannual insurance transactions will be measured on the basis of the annual insurance fees paid or collected.

**(4)** Negligible transactions at the subsidiaries – the transactions classified as negligible by the Company’s investees will be deemed as negligible at the Company level too, while those classified by them as non-negligible, will be examined on the Company level. In case that the Company does not have available information allowing the examination of the classification of transactions as negligible or non-negligible transactions, then the aggregate of all of the transactions of the same type will be deemed as a negligible or non-negligible transaction, except if according to the figures in the Company’s possession, one of the two conditions has been fulfilled: (1) According to the quantitative parameter above, the transaction in itself as a single transaction is not negligible; (2) the aggregate of the transactions is material to the Company.

**(5)** Non-quantitative examination – notwithstanding the aforesaid, the examination of the qualitative considerations of a negligible transaction from the quantitative aspect, may lead to the classification thereof as a transaction which is not negligible, if due to its nature, materiality and effect on the Company it is perceived as a significant event by the Company’s management and serves as a basis for adoption of important managerial decisions or if within the context of the Company’s transaction with controlling shareholders or another person in which the controlling shareholder has a personal interest, the other party is expected to receive benefits with regards to which there is significance in the reporting thereof to the investor public. It is clarified that even if a transaction of the Company with controlling shareholders or another person in which the controlling shareholder has a personal interest meets the quantitative test below, it will not be deemed negligible if such qualitative considerations indicate a material aspect thereof.

**The approving entity**

Pursuant to Section 22.3 of the Company’s articles, the Board determined that the classification of an interested parties’ transaction as a negligible transaction will be examined by the CFO in cooperation with the General Counsel, to the extent required, and in any approval of a transaction as negligible the examination and classification proceeding will be documented.

## Note 35 – Related and interested parties (Cont.)

### E. Negligible transactions: (Cont.)

**(5) (Cont.)**

**The approving entity (Cont.)**

In accordance with the Company’s master procedure, the classification of a transaction of the Company with controlling shareholders or with another person in which the Controlling Shareholder has a personal interest as a negligible transaction will be examined by the CFO and the General Counsel, to the extent required, and in every approval of a transaction as a negligible transaction, the examination and classification proceeding will be documented. In addition, the Board has authorized the Company's CEO or the CFO to approve the performance of transactions which meet the definition of negligibility according to this procedure, subject to the following two exceptions: (a) a situation in which both of the said persons have a personal interest in the same transaction, in which case such person will be replaced by another senior officer at the Company; and (b) a transaction concerning the terms of office and employment of an officer, or an engagement with a controlling shareholder or his relative, directly or indirectly, including through a company controlled by him, in respect of receipt of services from him by the Company, and if he is an employee of the Company and not an officer thereof – in respect of his employment at the Company, in which case the approval proceeding will be carried out pursuant to the Companies Law.

**Competitive proceeding or another proceeding**

In May 2015, the Audit Committee approved an amendment to the procedure, whereby unless decided otherwise by the Audit Committee, for Irregular Transactions and Non-negligible Transactions specified in Section 270(4) of the Companies Law, the Company's management shall conduct a competitive proceeding or another proceeding at the Company under the supervision of the Audit Committee, in accordance with the following principles.

In transactions for the purchase of services and/or the purchase of equipment and systems, the amount of annual expense in respect of which exceeds the quantitative threshold set for in the procedure, proposals from at least 3 different relevant suppliers in the required field, which were given in accordance with a specification of requirements to be determined thereby according to its needs and in accordance with the Group's procurement procedures, as being from time to time, will be presented to the Audit Committee with a recommendation to the Audit Committee of the chosen bidder and the reasons for the choice. The invitation to submit proposals will be supervised by the CFO of the Company who may instruct, according to his discretion, the performance of changes and/or improvements in the proceeding and/or negotiations with the bidders.

**Note 35 - Related and interested parties (Cont.)**

**E. Negligible transactions: (Cont.)**

**(5) (Cont.)**

**Competitive proceeding or another proceeding (Cont.)**

With respect to transactions for the lease of income-producing spaces, which are the Company's core business, and in view of the fact that during the regular course of business the proper proceeding is not necessarily a competitive proceeding, especially when such proceeding may create a business advantage for competing companies vis-à-vis potential lessees who are good for the Company, and the length of time for conducting such proceeding may jeopardize good transactions, the Company has adopted another proceeding, whereby a transaction, the amount of annual expense in respect of which exceeds the quantitative threshold set for in the procedure, and assuming that the marketing stages for such asset shall have commenced (i.e., pricing, hiring brokers etc.), the Company shall act to collect comparative data for the transaction (price per sqm, benefits and investments, lessees and their characterization, fittingness to the mix) in similar properties of the Company and similar properties of third parties in that area, and, to the extent required, shall be assisted by external consultants for this purpose. The Audit Committee and/or Board may request the Company's management to provide additional details or a comparison from other aspects. The Company's management shall present the Audit Committee with the details of the transaction proposed for approval and the reasons with respect to its advantageousness relative to the comparative transactions. It is clarified, that if it is a transaction which the Audit Committee determines to be uncharacteristic of the Company due to its scope and content (such as the construction or purchase of an entire building for the purpose of leasing it to one lessee which is a Related Party), the Audit Committee shall determine the procedures and the transaction shall be approved according to the requirements of the law.

Related Party Transactions for the purchase of products from companies owned by Granite Hacarmel, whose activity is not in the core business of the Group and their products are mostly sold "over the counter”, will not be deemed a transaction under the procedure.

Transactions with respect to terms of office and employment, other transactions with companies in the Granite Group and/or the contribution to bodies in which the Controlling Shareholder has a Personal Interest, shall be discussed at the Audit Committee, which shall determine, for every transaction, the suitable procedure for approval thereof. Nothing in the aforesaid shall derogate from the duties of approval of such engagements under any law.

In types of transactions in respect of which this chapter does not stipulate whether there is a duty to conduct a competitive proceeding or another proceeding, the Audit Committee shall determine in advance, ad hoc, for any concrete future transaction, whether the competitive proceeding or another proceeding will be conducted and the nature thereof as aforesaid.

**Supervision and audit**

Internal bi-quarterly review – until July 15 and January 15 of each year, a report shall be made to the Company's CFO on transactions as stated in the procedure (including negligible and non-negligible transactions) in which the Company engaged in the two quarters that lapsed, and in respect of transactions with affiliates in which other companies in the Group engaged, stating the terms and conditions of each transaction (annual financial volume, general financial volume, nature of the transaction, identity of the related party and other material conditions).

**Note 35 – Related and interested parties (Cont.)**

**E. Negligible transactions: (Cont.)**

**(5) (Cont.)**

**Annual follow-up**

Once a year, before the deliberation on the Company's annual financial statements, or in special cases if the Audit Committee so requests prior thereto, the coordinator will report to the Audit Committee on transactions as stated in the procedure (including negligible and non-negligible transactions and including the Company's engagements in lease agreements with related parties in view of the Company's undertaking in the Company's IPO prospectus released in May 2010) and in which the Company engaged during the previous year and during the months until the date of approval of the financial statement at the Company's institutions, insofar as relevant. The report will also include related party transactions in other companies of the Group which were brought to the coordinator’s attention during such period, stating the terms and conditions of each transaction (annual financial volume, general financial volume, nature of the transaction, identity of the related party and other material conditions), and regarding the sum total of the related party transactions in such year. In the framework of the annual follow-up as aforesaid, the officer shall attach a statement signed by him, whereby to the best of his knowledge and understanding, all of the relevant processes for mapping and identifying transactions with related parties were carried out at the Company and that all of the checks required by virtue of the undertaking in the prospectus were carried out, all in accordance with the provisions of the procedure, and that the transactions he reported were duly disclosed in the annual financial statements.

The Company's Board will examine, from time to time and at least once every three years, after receipt of the Audit Committee's recommendation, the implementation of the procedure by the Company and the need to update the procedure and/or the criteria therein and/or the proceedings prescribed for approval of the transactions, considering related party transactions in which the Company engages, material changes in the scope of the business of the Company and the Company’s investee companies, and the relevant financial figures, and changes in the relevant statutory provisions. The provisions of the procedure do not derogate from the authority of the Audit Committee to decide to hold a discussion, from time to time, on various aspects relating to interested party transactions and to invite to such discussions the relevant entities, including the Company's management, the coordinator, the internal auditor and the General Counsel.

After a discussion on the implementation of the provisions of the negligible transactions procedure and reviewing the consideration for the negligible transactions signed in 2018 and their other characteristics vis-à-vis the market conditions, which discussion was held on March 17, 2019 and March 19, 2019, the Audit Committee and the Board determined, respectively, that they were all transactions duly approved in 2018, including at the material companies controlled by the Company, and made under standard market conditions and have no material effect on the Company’s business position and results of operations. They further determined that all of the transactions examined as aforesaid were found to be transactions that meet the definition of “negligible transaction” in accordance with the Company’s procedure in respect of negligible transactions, and that this procedure was adequately implemented by the Company.

## Note 36 – Segment reporting

### A. General:

The Company applies IFRS 8, "Operating Segments" ("**IFRS 8**"). In accordance with the provisions of the standard, operating segments are identified on the basis of the internal reporting in respect of the components of the Group, which are reviewed on a regular basis by the Group's Chief Operational Decision Makers ("**CODM**") for the purpose of the allocation of resources and the evaluation of the performance of the operating segments.

The Company's business activities focus primarily on the various property segments, while most of the Group's business activity is in the retail centers and malls in Israel segment, and in the leasable office and other space segment, and land designated for residential lease in Israel. In addition, the Company engages in the income-producing property in the U.S. segment (office space for lease) and in the senior housing segment. In addition, the Company engages, through its holding (100%) in Granite in the marketing of energy substitutes (through Supergas Israeli Gas Distribution Company Ltd., held 100% by Granite), and through its holding (through Granite) in GES Global Environmental Solutions Ltd. in the field of the treatment of water, wastewater and chemicals.

The Company engages in additional activities, including financial investments and activity in the e-commerce sector which was acquired in June 2016.

The following are the Company's operating segments:

**Segment A** – Retail centers and malls in Israel.

**Segment B** – Leasable office and other space in Israel.

**Segment C** – Income-producing property in the U.S..

**Segment D** – Senior housing.

**Segment E** – Granite.

In the following business segments: the retail centers and malls in Israel, leasable office and other space in Israel, income-producing property in the U.S. and senior housing, the data of each one of the segments was aggregated.

Following are the considerations exercised by the management in implementing the criteria for aggregation of each one of these segment:

The Group's management examined the financial characteristics of each one of these segments and reached the conclusion that the financial characteristics in each one of them are similar, due to the fact that each one of the segments is managed in the same geographical region (Israel or the U.S.), stated in the same currency (NIS or USD), subject to similar political and legal conditions, and has similar profitability rates. In addition, the Group's management considered that each one of these segments is similar in all of the following characteristics:

- The nature of the projects – all of the projects in each one these segments are in the same operating segment.
- The nature of the development and enterprise processes – all of the projects in each one of these segments involve similar development and enterprise processes.
- Type of customers – all of the projects in each one of these segments, are marketed to similar clientele (business customers, the senior population).
- The methods used for marketing the projects – the methods for marketing all of the projects in each one of these segments are similar and include identical advertising and marketing processes.

**Note 36 – Segment reporting (Cont.)**

**A. General (Cont.)**

- The nature of the supervisory environment – similar laws, regulations and rules apply to all of the projects in each one of these segments, including in respect of real property, planning, construction, and leasing, environmental protection, laws on the municipal level and in respect of land taxation, and laws and regulations in the field of senior housing.

Based on the considerations specified above, the Group's management believes that the aggregation of each one of the segments: the retail centers and malls in Israel, leasable office and other space in Israel, income-producing property in the U.S. and senior housing are in accordance with IFRS 8.

**Note 36 – Segment reporting (Cont.)**

**B. Operating segments:**

| | For the year ended December 31, 2018 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Retail centers and malls in Israel | Leasable office and other space in Israel | Income-producing property in the U.S. | Senior housing | Granite | Others | Consolidated |
| | | | | NIS in millions | | | |
| **Income:** | | | | | | | |
| Total external income | 1,034 | 633 | 267 | 130 | 720 | 37 | ,2821 |
| **Total segment expenses** | 214 | 116 | 118 | 93 | 603 | 90 | 1,234 |
| **Segment profit (loss) (NOI)** | 820 | 517 | 149 | 37 | 117 | (53) | ,1587 |
| **Net profit (loss) from adjustment to fair value of investment property and investment property under construction** | (4) | 167 | (48) | 103 | - | - | 218 |
| Unallocated costs | | | | | | | (132) |
| Financing expenses, net | | | | | | | (241) |
| Other income, net | | | | | | | 88 |
| Company's share in the results of associates, net of tax | | | | | | | (6) |
| **Income before taxes on income** | | | | | | | ,1514 |
| **Additional information as of December 31, 2018:** | | | | | | | |
| Segment assets | 12,682 | 10,443 | 2,593 | 2,081 | 1,225 | | 29,024 |
| Unallocated assets (*) | | | | | | | 2,871 |
| Total consolidated assets | | | | | | | 31,895 |
| Capital investments | 318 | 836 | 474 | 236 | 47 | | |

(*) Mainly financial assets (including ones held for sale) in the sum of approx. NIS 1.7 billion and cash and short-term deposits in the sum of NIS 0.7 billion.

## Note 36 – Segment reporting (Cont.)

### B. Operating segments (Cont.):

| | For the year ended December 31, 2017 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Retail centers and malls in Israel | Leasable office and other space in Israel | Income-producing property in the U.S. | Senior housing | Granite | Others | Consolidated |
| | NIS in millions | | | | | | |
| **Income:** | | | | | | | |
| Total external income | 1,032 | 489 | 221 | 126 | 705 | 19 | 2,592 |
| **Total segment expenses** | 204 | 92 | 100 | 87 | 601 | 65 | 1,149 |
| **Segment profit (loss) (NOI)** | 828 | 397 | 121 | 39 | 104 | (46) | 1,443 |
| **Net profit (loss) from adjustment to fair value of investment property and investment property under construction** | (25) | 630 | (186) | 81 | - | - | 500 |
| Unallocated costs | | | | | | | (115) |
| Financing expenses, net | | | | | | | (90) |
| Other income, net | | | | | | | 124 |
| Company's share in the results of associates, net of tax | | | | | | | (6) |
| **Income before taxes on income** | | | | | | | 1,856 |
| **Additional information as of December 31, 2017:** | | | | | | | |
| Segment assets | 12,368 | 9,462 | 1,983 | 1,725 | 1,265 | | 26,803 |
| Unallocated assets (*) | | | | | | | 3,340 |
| Total consolidated assets | | | | | | | 30,143 |
| Capital investments | 321 | 598 | 191 | 138 | 51 | | |

(*) Mainly financial assets in the sum of approx. NIS 1.7 billion and cash and short-term deposits in the sum of NIS 1.1 billion.

## Note 36 – Segment reporting (Cont.)

### B. Operating segments: (Cont.)

| | For the year ended December 31, 2016 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Retail centers and malls in Israel | Leasable office and other space in Israel | Income-producing property in the U.S. | Senior housing | Granite | Others | Consolidated |
| | NIS in millions | | | | | | |
| **Income:** | | | | | | | |
| Total external income | 974 | 447 | 229 | 95 | 653 | 7 | 2,405 |
| **Total segment expenses** | 195 | 78 | 105 | 66 | 570 | 12 | 1,026 |
| **Segment profit (loss) (NOI)** | 779 | 369 | 124 | 29 | 83 | (5) | 1,379 |
| **Net profit (loss) from adjustment to fair value of investment property and investment property under construction** | 220 | 517 | (82) | 56 | - | - | 711 |
| Unallocated costs | | | | | | | (115) |
| Financing expenses, net | | | | | | | (110) |
| Other income, net | | | | | | | 9 |
| Company's share in the results of associates, net of tax | | | | | | | (8) |
| **Income before taxes on income** | | | | | | | 1,866 |
| **Additional information as of December 31, 2016:** | | | | | | | |
| Segment assets | 12,074 | 8,219 | 2,176 | 1,495 | 1,298 | | 25,262 |
| Unallocated assets (*) | | | | | | | 3,321 |
| Total consolidated assets | | | | | | | 28,583 |
| Capital investments | 639 | 1,038 | 233 | 638 | 43 | | |

(*) Mainly financial assets in the sum of approx. NIS 1.6 billion and cash and short-term deposits in the sum of NIS 1.3 billion.

**Note 37 - Material subsequent events**

**A.** According to a Board resolution of March 19, 2019, it has been resolved to distribute a dividend in the total amount of NIS 560 million.

**B.** For details regarding the issuance of the Series E and F Bonds after the date of the Statement of Financial Position, see Note 19B(4).

**C.** For details with respect to the sale of shares in Bank Leumi Le-Israel Ltd. after the date of the Statement of Financial Position, see Note 11A.

**D.** For details with respect to the closing of the sale of Leumi Card after the date of the Statement of Financial Position, see Note 11B.

**E.** For updates on claims after the date of the Statement of Financial Position - see Note 31 regarding contingent liabilities.

# Azrieli Group Ltd.

**Separate Financial Information**
**For Y2018**

**Prepared pursuant to the provisions of Section 9C of the Securities Regulations**
**(Periodic and Immediate Reports), 5730-1970**

# Azrieli Group Ltd.

**Separate Financial Information**
**For Y2018**

**C o n t e n t s**

Deloitte.

To
The Shareholders of
**Azrieli Group Ltd.**
1 Azrieli Center
Tel Aviv

Dear Sir/Madam,

**Re: Auditor's special report on separate financial information pursuant to Regulation 9C of the Securities Regulations (Periodic and Immediate Reports), 5730-1970**

We have audited the separate financial information, which is presented according to Regulation 9C of the Securities Regulations (Periodic and Immediate Reports), 5730-1970, of Azrieli Group Ltd. (the "**Company**") as of December 31, 2018 and 2017 and for each of the years in the three-year period ended December 31, 2018. The Company's Board and Management are responsible for this separate financial information. Our responsibility is to express an opinion on this separate financial information based on our audit.

We did not audit the separate financial information from the financial statements of investee companies, the total investments in which amounted to approx. NIS 377 million and approx. NIS 307 million as of December 31, 2018 and 2017, respectively, and the income from continuing operations from such investee companies amounted to approx. NIS 68 million, approx. NIS 66 million and approx. NIS 48 million for the years ended on December 31, 2018, 2017 and 2016, respectively, and loss from discontinued operations from such investee companies which amounted to approx. NIS 2 million and approx. NIS 9 million for the years ended on December 31, 2018 and 2016, respectively. The financial statements of such companies were audited by other auditors whose reports were furnished to us, and our opinion, insofar as it relates to the amounts that have been included in respect of such companies, is based upon the reports of the other auditors.

We performed our audit in accordance with generally accepted auditing standards in Israel. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the separate financial information is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and details included in the separate financial information. An audit also includes assessing the accounting principles used in the preparation of the separate financial information and significant estimates made by the Company's Board and Management, as well as evaluating the overall separate financial information presentation. We believe that our audit and the other auditors' reports provide a reasonable basis for our opinion.

In our opinion, based on our audit and on the reports of other auditors, the separate financial information was prepared, in all material respects, according to the provisions of Regulation 9C of the Securities Regulations (Periodic and Immediate Reports), 5730-1970.

**Brightman, Almagor, Zohar & Co.**
**Certified Public Accountants**
**Member of Deloitte Touche Tohmatsu Limited**

**Tel Aviv, March 19, 2019**



**Tel Aviv - Main Office**
1 Azrieli Center Tel Aviv, 6701101 P.O.B. 16593
Tel Aviv, 6116402 | Tel: +972 (3) 608 5555 | Fax: +972 (3) 609 4022 | info@deloitte.co.il

**Jerusalem**
3 Kiryat Ha'Mada
Har Hotzvim Tower
Jerusalem, 9777603
Delivery Box 45396
Jerusalem 9145101
Tel: +972 (2) 501 8888
Fax: +972 (2) 537 4173
info-jer@deloitte.co.il

**Haifa**
5 Ma'aleh Hashichrur
P.O.B. 5648
Haifa, 3105502
Tel: +972 (4) 860 7333
Fax: +972 (4) 867 2528
info-haifa@deloitte.co.il

**Beer Sheva**
12 Alumot
Omer Industrial Park
P.O.B 1369
Omer, 8496500
Tel: +972 (8) 690 9500
Fax: +972 (8) 690 9600
info-beersheva@deloitte.co.il

**Eilat**
The City Center
P.O.B 583
Eilat, 8810402
Tel: +972 (8) 637 5676
Fax: +972 (8) 637 1628
info-eilat@deloitte.co.il

**Trigger Foresight A Deloitte Israel Company**
3 Azrieli Center
Tel Aviv, 6701101
Tel: +972 (3) 607 0500
Fax: +972 (3) 607 0501
info@deloitte.co.il

**Deloitte Analytics**
7 Hasivim
P.O.B. 7796
Petah Tikva, 4959368
Tel: +972 (77) 8322221
Fax: +972 (3) 9190372
info@deloitte.co.il

**Seker - Deloitte**
7 Giborey Israel St.
P.O.B 8458
Netanya 4250407
Tel: +972 (9) 892 2444
Fax: +972 (9) 892 2440
info-seker@deloitte.co.il

# Azrieli Group Ltd.

## Information on the Financial Position

| | As of December 31 | |
|---|---|---|
| | 2018 | 2017 |
| | NIS in millions | NIS in millions |
| **Assets** | | |
| **Current assets** | | |
| Cash and cash equivalents | 372 | 826 |
| Short-term deposits and investments | 1 | 101 |
| Trade accounts receivable | 13 | 14 |
| Other receivables | 136 | 96 |
| Current tax assets | 62 | 5 |
| | 584 | 1,042 |
| Assets held for sale | 450 | 40 |
| **Total current assets** | 1,034 | 1,082 |
| **Non-current assets** | | |
| Financial assets | 1,227 | 1,685 |
| Investment property and investment property under construction | 11,401 | 10,397 |
| Investments in investee companies | 9,327 | 8,610 |
| Loans to investee companies | 3,755 | 3,711 |
| Fixed assets | 9 | 9 |
| Receivables | 36 | 18 |
| **Total non-current assets** | 25,755 | 24,430 |
| **Total assets** | 26,789 | 25,512 |
| **Liabilities and capital** | | |
| **Current liabilities** | | |
| Credit and current maturities from financial corporations and bonds | 1,291 | 1,413 |
| Trade payables | 132 | 88 |
| Payables and other current liabilities | 68 | 89 |
| **Total current liabilities** | 1,491 | 1,590 |
| **Non-current liabilities** | | |
| Loans from financial corporations | 904 | 1,095 |
| Bonds | 5,886 | 5,122 |
| Other liabilities | 26 | 18 |
| Deferred tax liabilities | 1,405 | 1,406 |
| **Total non-current liabilities** | 8,221 | 7,641 |
| **Capital** | | |
| Ordinary share capital | 18 | 18 |
| Share premium | 2,478 | 2,478 |
| Capital reserves | 674 | 571 |
| Retained earnings | 13,907 | 13,214 |
| **Total capital attributed to shareholders of the Company** | 17,077 | 16,281 |
| **Total liabilities and capital** | 26,789 | 25,512 |

| **March 19, 2019** | | | |
|---|---|---|---|
| **Date of approval of the separate financial information** | **Danna Azrieli**<br>**Chairman of the Board** | **Eyal Henkin**<br>**CEO** | **Irit Sekler-Pilosof**<br>**Chief Financial Officer** |

# Azrieli Group Ltd.

## Information on the Income or Other Comprehensive Loss and Profit

| | For the year ended December 31 | | |
|---|---|---|---|
| | 2018 | 2017 | 2016 |
| | NIS in millions | NIS in millions | NIS in millions |
| **Revenues** | | | |
| From rent and management and maintenance fees | 629 | 514 | 471 |
| Net profit from adjustment to fair value of investment property and investment property under construction | 176 | 455 | 614 |
| Financing | 147 | 215 | 188 |
| Other | 90 | 63 | 10 |
| **Total revenues** | 1,042 | 1,247 | 1,283 |
| **Costs and expenses** | | | |
| Cost of revenues from rent and management and maintenance fees | 27 | 21 | 14 |
| Sales and marketing | 29 | 26 | 23 |
| General and administrative | 59 | 53 | 51 |
| Financing | 159 | 104 | 91 |
| Other | 3 | - | - |
| **Total costs and expenses** | 277 | 204 | 179 |
| **Profit before Company's share in the profits of investee companies** | 765 | 1,043 | 1,104 |
| Share in profits of investee companies, net of tax | 574 | 642 | 814 |
| **Profit before income taxes** | 1,339 | 1,685 | 1,918 |
| Taxes on income | (119) | (229) | (99) |
| **Net profit for the year from continuing operations** | 1,220 | 1,456 | 1,819 |
| Loss from discontinued operations (after tax) | (2) | - | (9) |
| **Net profit for the year** | 1,218 | 1,456 | 1,810 |
| **Other comprehensive income:** | | | |
| **Amounts that will not be classified in the future to income or loss, net of tax:** | | | |
| Change in fair value of financial assets, net of tax | 11 | 204 | 106 |
| **Amounts that were or will be classified in the future to income or loss, net of tax:** | | | |
| Translation differences due to foreign operations | 67 | (81) | (9) |
| Amounts carried to the income statement from disposition of financial assets, net of tax | - | (62) | (20) |
| Share in the other comprehensive income (loss) of investee companies, net of tax. | 25 | (29) | 8 |
| **Total** | 92 | (172) | (21) |
| **Other comprehensive income for the year, net of tax** | 103 | 32 | 85 |
| **Total comprehensive income for the year** | 1,321 | 1,488 | 1,895 |

# Azrieli Group Ltd.

## Information on the Cash Flows

| | For the year ended December 31 | | |
|---|---|---|---|
| | 2018 | 2017 | 2016 |
| | NIS in millions | NIS in millions | NIS in millions |
| **Cash flows - current operations** | | | |
| Net profit for the year | 1,218 | 1,456 | 1,810 |
| Depreciation and amortization | 2 | 1 | 1 |
| Net profit from adjustment of fair value of investment property and investment property under construction | (176) | (455) | (614) |
| Financing and other income, net | (85) | (180) | (103) |
| Share in profits of investee companies, net of tax | (572) | (642) | (805) |
| Tax expenses recognized in the income statement | 119 | 229 | 99 |
| Income tax paid, net | (153) | (68) | (88) |
| Change in trade and other receivables | (69) | 1 | 51 |
| Change in trade and other payables | 8 | (7) | 14 |
| Change in employee provisions and benefits | 2 | - | 1 |
| Erosion (revaluation) of financial assets designated at fair value through profit and loss | 8 | 4 | (4) |
| Receipt of deposits from senior housing tenants | - | - | 2 |
| **Net cash – current operations** | 302 | 339 | 364 |
| | | | |
| **Cash flows - investment activities** | | | |
| Proceeds from liquidation of fixed assets | - | - | 36 |
| Acquisition and investment in investment property and investment property under construction | (770) | (486) | (1,263) |
| Purchase of fixed assets | (2) | (3) | (38) |
| Investments in investee companies | (87) | (80) | (110) |
| Proceeds from financial assets designated at fair value through profit and loss, net | - | 3 | 5 |
| Receipt (Granting) of long-term loans to investee companies, net | (101) | 183 | (290) |
| Acquisition of investee companies | - | - | (99) |
| Interest and dividend received | 114 | 57 | 34 |
| Return of investment in an investee company | 14 | 12 | 2 |
| Proceeds from liquidation of financial assets, net | - | 233 | 80 |
| Change in short-term deposits | 100 | 511 | (611) |
| Taxes paid in respect of financial assets | (2) | (17) | - |
| Proceeds from disposition of investment property | 31 | 8 | - |
| **Net cash - investment activities** | (501) | 421 | (2,254) |

# Azrieli Group Ltd.

## Information on the Cash Flows
**(Continued)**

| | For the year ended December 31 | | |
|---|---|---|---|
| | 2018 | 2017 | 2016 |
| | NIS in millions | NIS in millions | NIS in millions |
| **Cash flows - financing activities** | | | |
| Issue of bonds net of issue expenses | 1,399 | 1,354 | 2,177 |
| Dividend distribution to the shareholders | (520) | (480) | (400) |
| Repayment of bonds | (454) | (609) | (167) |
| Receipt of long-term loans from financing corporations | - | - | 800 |
| Repayment of long-term loans from financing corporations | (422) | (473) | (770) |
| Short-term credit from financing corporations, net | (146) | (74) | 45 |
| Customer deposits, net | - | 1 | 1 |
| Interest paid | (113) | (102) | (103) |
| **Net cash - financing activities** | (256) | (383) | 1,583 |
| **Increase (decrease) in cash and cash equivalents** | (455) | 377 | (307) |
| Cash and cash equivalents at the beginning of the year | 826 | 454 | 761 |
| Effect of exchange rates changes on cash balances held in foreign currency | 1 | (5) | - |
| **Cash and cash equivalents at the end of the year** | 372 | 826 | 454 |

(*) Non-cash activities include increase in payables balances due to credit purchases of non-current assets for 2018 in the amount of NIS 14 million (in 2017 and 2016 – NIS 32 million and NIS 5 million, respectively).

# Azrieli Group Ltd.

## Additional Information for the Separate Financial Statements

**A. General:**

**Definitions**

| | | |
|---|---|---|
| **The Company** | - | Azrieli Group Ltd. |
| **Investee company** | - | See Note 9 to the Company's Consolidated Financial Statements as of December 31, 2018. |

**B. Form of Preparation of the Financial Information:**

The financial information out of the Consolidated Statements, attributed to the Company itself as a parent company (the "Financial Information") were prepared according to the provisions of Regulations 9C of and the 10$^{th}$ Schedule to the Securities Regulations (Periodic and Immediate Reports), 5730-1970.

The Notes specified below also include disclosures pertaining to additional material information, according to the disclosure requirements specified in the said Regulation and as specified in the 10$^{th}$ Schedule, insofar as such information is not included in the Consolidated Statements in a manner which explicitly addresses the Company itself as a parent company.

**(1) Accounting policy**

The Company's separate financial information is prepared according to the accounting policy specified in Note 2 to the Company's Consolidated Financial Statements except for the amounts of the assets, liabilities, revenues, expenses and cash flows in respect of investee companies, as specified below:

**a.** The assets and liabilities are presented at their value in the consolidated statements attributed to the Company itself as a parent company, except for investments in investee companies.

**b.** Investments in investee companies are presented as the net sum amount of the total assets net of the total liabilities which present in the Company's consolidated statements financial information regarding the investee companies, including goodwill.

**c.** The revenues and expenses amounts reflect the revenues and expenses included in the consolidated statements attributed to the Company itself as a parent company, segmented between profit or loss and other comprehensive income, except for amounts of revenues and expenses in respect of investee companies.

**d.** The Company's share in the results of investee companies is presented as the net amount of the total revenues net of the total expenses presenting in the consolidated statements of the Company business results in respect of investee companies, including impairment of goodwill or the reversal thereof, in segmentation between profit or loss and other comprehensive income.

**e.** The cash flow amounts reflect the amounts included in the consolidated statements attributed to the Company itself as a parent company, except for amounts of the cash flows in respect of investee companies.

**f.** Loans given and/or received from investee companies are presented at the amount attributed to the Company itself as a parent company.

**g.** Balances, revenues and expenses in respect of transactions with investee companies which were written off within the consolidated statements, are measured and presented within the relevant clauses in the information on the financial position and the comprehensive income, in the same manner that such transactions would have been measured and presented had they been performed vis-à-vis third parties. Profits (losses) in respect of such transactions until the level that they are not recognized in the Company's consolidated statements, which were deferred, are presented net of (as an addition) of the items of the Company's share in the profits (losses) of investee companies and investments in investee companies so that the Company's separate profit (loss) is identical to the Company's consolidated profit (loss) attributed to the owners of the parent company.

**C. Financial Assets and Liabilities:**

**(1) Liquidity risk management**

**Financial liabilities which do not constitute derivative financial instruments:**

The following tables specify the Company's remaining contractual maturity dates in respect of financial liabilities which do not constitute a derivative financial instrument. The tables were prepared based on the non-discounted cash flows of the financial liabilities based on the earliest date on which the Company might be required to repay them. The table includes cash flows in respect of both interest and principal.

| | As of December 31, 2018 | | | | | |
|---|---|---|---|---|---|---|
| | Book Value | Projected cash flow | 2019 | 2020 | 2021 | 2022 forth |
| | NIS in millions | | | | | |
| **Financial liabilities which are not derivatives** | | | | | | |
| Short-term credit from financing corporations (1) | 456 | 456 | 456 | - | - | - |
| Trade accounts payable | 132 | 132 | 132 | - | - | - |
| Other payables | 14 | 14 | 14 | - | - | - |
| Loans from financing corporations (2) | 1,109 | 1,159 | 218 | 322 | 186 | 433 |
| Bonds (2) | 6,560 | 7,044 | 722 | 714 | 706 | 4,902 |
| Long-term customer deposits | 23 | 23 | - | - | 23 | - |
| **Total** | 8,294 | 8,828 | 1,542 | 1,036 | 915 | 5,335 |

| | As of December 31, 2017 | | | | | |
|---|---|---|---|---|---|---|
| | Book Value | Projected cash flow | 2018 | 2019 | 2020 | 2021 forth |
| | NIS in millions | | | | | |
| **Financial liabilities which are not derivatives** | | | | | | |
| Short-term credit from financing corporations (1) | 602 | 602 | 602 | - | - | - |
| Trade accounts payable | 88 | 88 | 88 | - | - | - |
| Other payables | 30 | 30 | 30 | - | - | - |
| Loans from financing corporations (2) | 1,522 | 1,592 | 443 | 217 | 319 | 613 |
| Bonds (2) | 5,545 | 6,018 | 466 | 588 | 582 | 4,382 |
| Long-term customer deposits | 17 | 17 | - | - | 17 | - |
| **Total** | 7,804 | 8,347 | 1,629 | 805 | 918 | 4,995 |

(1) Book value includes interest accrued as of December 31, 2018 and 2017.
(2) Book value includes current maturities and interest accrued as of December 31, 2018 and 2017.

**C. Financial Assets and Liabilities (Contd.):**

**(2) Details regarding investments in other companies at fair value through other comprehensive income:**

**Details regarding investments in financial assets available for sale**

For details pertaining to the Company's investments in Bank Leumi Le-Israel Ltd. and Leumi Card Ltd., see Note 11 to the Consolidated Financial Statements as of December 31, 2018.

**D. Taxes on Income:**

**(1) Details regarding the tax environment in which the Group operates and changes in the tax rates:**

For details pertaining to the tax environment in which the Company operates, see Note 28A to the Consolidated Financial Statements for the year ended on December 31, 2018.

**(2) Taxes on income recognized in profit and loss:**

| | For the year ended on December 31 | | |
|---|---|---|---|
| | **2018** | **2017** | **2016** |
| | **NIS in millions** | **NIS in millions** | **NIS in millions** |
| **Current taxes:** | | | |
| For the current period | (40) | (74) | (62) |
| Adjustments for previous years, net | (62) | 6 | - |
| | (104) | (68) | (62) |
| **Deferred taxes expenses:** | (17) | (161) | (37) |
| **Total income tax expenses** | (119) | (229) | (99) |

**(3) Tax Assessments:**

See Note 28F to the Consolidated Financial Statements of the year ended on December 31, 2018.

**D. Taxes on Income: (Cont.)**

**(4) Taxes on income due to other comprehensive income components:**

| | 2018 | | | 2017 | | | 2016 | | |
|---|---|---|---|---|---|---|---|---|---|
| | Amounts before tax | Tax income (expense) | Amounts net of tax | Amounts before tax | Tax income (expense) | Amounts net of tax | Amounts before tax | Tax income (expense) | Amounts net of tax |
| | NIS in millions | | | | | | | | |
| Change in the fair value of financial assets | - | 11 | 11 | 269 | (65) | 204 | 124 | (18) | 106 |
| Amounts carried to the income statement from disposition of financial assets | - | - | - | (81) | 19 | (62) | (26) | 6 | (20) |
| Translation differences due to foreign operations | 67 | - | 67 | (81) | - | (81) | (9) | - | (9) |
| Share in the other comprehensive income (loss) of investee companies, net of tax | 25 | - | 25 | (29) | - | (29) | 8 | - | 8 |
| Total other comprehensive income (loss) | 92 | 11 | 103 | 78 | (46) | 32 | 97 | (12) | 85 |

(*) The deferred taxes were calculated in 2018 and 2017 according to a tax rate of 23% (in 2016 according to a tax rate of 23%-24%).

**D. Taxes on Income: (Cont.)**

**(5) Deferred taxes note:**

**Deferred taxes assets and liabilities which were recognized**

The deferred taxes are calculated according to the tax rate expected to apply on the reversal date as specified above.

Deferred taxes assets and liabilities are attributed to the following items:

| | Real estate assets and fixed assets | Employee benefits | Financial instruments (1) | Carry forward deductions and losses for tax purposes | Others (2) | Total |
|---|---|---|---|---|---|---|
| | NIS in millions | NIS in millions | NIS in millions | NIS in millions | NIS in millions | NIS in millions |
| **Deferred tax asset (liability) balance as of January 1, 2017** | (1,162) | 1 | (97) | 9 | 50 | (1,199) |
| Changes carried to profit and loss | (140) | - | (7) | (9) | (6) | (162) |
| Changes carried to other comprehensive income | - | - | (46) | - | - | (46) |
| Effect of tax rate changes recognized in profit and loss | 1 | - | - | - | - | 1 |
| **Deferred tax asset (liability) balance as of December 31, 2017** | (1,301) | 1 | (150) | - | 44 | (1,406) |
| Changes carried to profit and loss | (98) | - | 8 | 86 | (13) | (17) |
| Changes carried to other comprehensive income | - | - | 11 | - | - | 11 |
| Other | - | - | - | - | 7 | 7 |
| **Deferred tax asset (liability) balance as of December 31, 2018** | (1,399) | 1 | (131) | 86 | 38 | (1,405) |

**(1)** Mainly due to financial assets available for sale.

**(2)** Mainly due to the capital reserve created due to credit given to subsidiaries other than at arm's length.

**E. Material Engagements and Transactions with Investee Companies:**

**(1)** On material investments in companies directly held by the Company, see Note 9 to the Consolidated Financial Statements as of December 31, 2018.

**(2)** **a.** Canit Hashalom Investments Ltd. ("**Canit Hashalom**") issued to the Company bonds in the amount of NIS 1,220 million, linked to the Consumer Price Index (the "**CPI**"). The linkage differentials in respect of the loan will in any event not be lower than the interest set in respect of Section 3(j) of the Income Tax Ordinance. In 2018 NIS 380 million (in nominal terms) have been paid up out of the said bond series. The balance of the principal and linkage differentials will be repaid in a single installment on December 31, 2018 and if Canit Hashalom does not pay the principal, the interest and the linkage differentials by the maturity date, the bonds shall be deemed as having been paid and reissued on the day following the maturity date. The balance, as of December 31, 2018, is NIS 1,021 million.

**b.** Canit Hashalom issued to the Company bonds in the amount of NIS 1,080 million linked to the CPI and bearing interest at a rate of 1% per annum. The interest and the linkage differentials in respect of the loan will in any event not be lower than the interest determined for purposes of Section 3(j) of the Income Tax Ordinance. The principal, interest and linkage differentials will be repaid in one sum on December 31, 2018. In case that Canit Hashalom will not pay the principal, interest and linkage differentials until the maturity date, the bonds shall be deemed as having been paid and reissued on the day following the maturity date. The balance as of December 31, 2018 is NIS 1,444 million.

In addition, the Company provided loans without a maturity date to Canit Hashalom, the balance of which as of December 31, 2018, is approx. NIS 20 million, which are not linked to the CPI and bear interest according to the Income Tax Regulations.

The credit is presented and measured at fair value on the date of first recognition, according to the current value of the projected returns. The difference between the fair value measured on the date of first recognition and the loan amount actually granted, is carried to a capital reserve from transactions with a controlling shareholder. The balance of the liability due to the capital fund from transactions with controlling shareholders as of December 31, 2018 is approx. NIS 91 million (December 31, 2017 – approx. NIS 121 million).

**(3) Material arrangements between the Company and Investee Companies**

**a.** The Company and several companies held thereby and other companies in the Group have agreements, according to which the Company is entitled to management fees at a fixed rate out of those companies' total expenses. In the years 2018 and 2017, the Company received management fees as aforesaid at a total sum of approx. NIS 31 million and approx. NIS 28 million, respectively.

**b.** The Company and several companies held thereby have agreements, according to which the Company is entitled to amounts for a depreciation and replacement fund for the replacement and/or fundamental repair of facilities and equipment serving all of the tenants in the Company's real estate. In the years 2018 and 2017, the Company received proceeds as aforesaid in a total amount of approx. NIS 11 million.

**c.** The Company and several companies held thereby have agreements, according to which the Company is entitled to amounts for rent due to the companies' use of areas owned thereby. In the years 2018 and 2017, the Company received rent as aforesaid in a total amount of approx. NIS 2 million.

**E. Material engagements and transactions with investee companies: (Cont.)**

**(3) Material arrangements between the Company and Investee Companies (Cont.)**

**d.** The Company provided loans to several investee companies thereof, as detailed below:

Loans in an amount of approx. NIS 154 million linked to the USD and bearing interest at a rate of approx. 10% per annum.

A loan in an amount of approx. NIS 45 million linked to the USD and bearing interest at a rate of approx. 6.5% per annum.

A loan in an amount of approx. NIS 24 million linked to the USD and bearing interest at a rate of approx. 6% per annum.

Capital notes in the amount of approx. NIS 997 million linked to the CPI and bearing no interest for a period of 5 years. The balance is presented net of capital reserve.

With regards to the loans to Canit Hashalom, see Section 2 above.

The remaining loans bear interest pursuant to the Income Tax Regulations.

The interest and linkage differentials which were accrued due to such loans and were presented in the Statement of Net Profit of the Company for the years ended on December 31, 2018 and 2017 are in a total amount of approx. NIS 148 million and approx. NIS 133 million, respectively.

**e.** The Company bears expenses for office, insurance, compensation and benefits of senior employees at the group (the "**Group's Expenses**"). The Company and several companies held thereby and other companies in the Group have agreements, according to which the Company is entitled to reimbursement for amounts paid thereby for the companies. In the years 2018 and 2017 the Company received such proceeds in a total amount of approx. NIS 27 million and approx. NIS 29 million, respectively.

**f.** The Company and companies held thereby have an agreement, according to which the investee companies are entitled to rent, management fee and parking fees for areas owned thereby. In the years 2018 and 2017, the Company paid rent, management fees and parking fees as aforesaid in a total amount of approx. NIS 6 million and approx. NIS 5 million, respectively.

**F. Guarantees:**
For details on guarantees provided by the Company – See Note 30B to the Consolidated Financial Statements as of December 31, 2018.

**G. Contractual Restrictions and Financial Covenants:**
For details regarding contractual restrictions undertaken by the Company, see Note 19 to the Consolidated Financial Statements as of December 31, 2018.

**H. Dividends from Companies Directly held by the Company:**
Companies directly held by the Company have no contractual restrictions on dividend distribution.

**I. Pledges:**
With respect to pledges – see Note 30A to the Consolidated Financial Statements as of December 31, 2018.

**J. Engagements with Affiliated and Interested Parties:**
Regarding engagements with related and interested parties, see Note 35 to the Consolidated Financial Statements as of December 31, 2018.

**K. Subsequent Events:**
Regarding subsequent material events, see Note 37 to the Consolidated Financial Statements as of December 31, 2018.

Deloitte.

Date: March 19, 2019
Our number: 155996

The Board of Directors of Azrieli Group Ltd.
1 Azrieli
Tel Aviv

**Dear Sir/Madam,**

**Re: Consent in Connection with the Shelf Prospectus of Azrieli Group Ltd. of May 2016**

We hereby notify you that we agree to the inclusion (including by way of reference) of our reports that are specified below in connection with the shelf prospectus of May 2016:

(1) Auditor's report of March 19, 2019 on the consolidated financial statements of the Company as of December 31, 2018 and 2017 and for each of the three years in the period ended December 31, 2018.

(2) Auditor's report of March 19, 2019 on the audit of components of internal control over the financial reporting of the Company as of December 31, 2018.

(3) Special auditor's report of March 19, 2019 on separate financial information of the Company pursuant to Section 9C of the Securities Regulations (Periodic and Immediate Reports), 5730-1970 as of December 31, 2018 and 2017 and for each of the three years in the period ended December 31, 2018.

Sincerely,

**Brightman Almagor Zohar & Co.**
**Certified Public Accountants**
**Member of Deloitte Touche Tohmatsu Limited**

**Tel Aviv - Main Office**
1 Azrieli Center Tel Aviv, 6701101 P.O.B. 16593
Tel Aviv, 6116402 | Tel: +972 (3) 608 5555 | Fax: +972 (3) 609 4022 | info@deloitte.co.il

**Jerusalem**
3 Kiryat Ha'Mada
Har Hotzvim Tower
Jerusalem, 9777603
Delivery Box 45396
Jerusalem 9145101
Tel: +972 (2) 501 8888
Fax: +972 (2) 537 4173
info-jer@deloitte.co.il

**Haifa**
5 Ma'aleh Hashichrur
P.O.B. 5648
Haifa, 3105502
Tel: +972 (4) 860 7333
Fax: +972 (4) 867 2528
info-haifa@deloitte.co.il

**Beer Sheva**
12 Alumot
Omer Industrial Park
P.O.B 1369
Omer, 8496500
Tel: +972 (8) 690 9500
Fax: +972 (8) 690 9600
info-beersheva@deloitte.co.il

**Eilat**
The City Center
P.O.B 583
Eilat, 8810402
Tel: +972 (8) 637 5676
Fax: +972 (8) 637 1628
info-eilat@deloitte.co.il

**Trigger Foresight A Deloitte Israel Company**
3 Azrieli Center
Tel Aviv, 6701101
Tel: +972 (3) 607 0500
Fax: +972 (3) 607 0501
info@deloitte.co.il

**Deloitte Analytics**
7 Hasivim
P.O.B. 7796
Petah Tikva, 4959368
Tel: +972 (77) 8322221
Fax: +972 (3) 9190372
info@deloitte.co.il

**Seker - Deloitte**
7 Giborey Israel St.
P.O.B 8458
Netanya 4250407
Tel: +972 (9) 892 2444
Fax: +972 (9) 892 2440
info-seker@deloitte.co.il

# Further Details about the Corporation

# Part D

# CHAPTER D | ADDITIONAL DETAILS ABOUT THE CORPORATION

# CHAPTER D | ADDITIONAL DETAILS ABOUT THE CORPORATION

## Regulation 25A – Registered Address

Company Name: Azrieli Group Ltd.

Company Number in the Registrar of Companies: 51-096071-9

Address: 1 Azrieli Center, Tel Aviv, 6702101

Facsimile: 03-6081380

Telephone: 03-6081400

email: rant@azrieli.com

Date of the Statement of Financial Position: December 31, 2018

The Report Date: March 19, 2019

## Regulation 10A - Summary of the Reports on Results of the Company's Operations for Each Quarter of 2018 (NIS in million)

| | 1-3/2018 | 4-6/2018 | 7-9/2018 | 10-12/2018 | 1-12/2018 |
|---|---|---|---|---|---|
| Income | | | | | |
| From rent, management and maintenance fees | 493 | 507 | 530 | 533 | 2,063 |
| From sales, work and services | 215 | 171 | 162 | 210 | 758 |
| Profit (loss), net of fair value adjustment of investment properties and properties under construction | (38) | 15 | (13) | 254 | 218 |
| Financing | 8 | 2 | 4 | 3 | 17 |
| Other | 22 | 15 | 33 | 25 | 95 |
| Total Income | 700 | 710 | 716 | 1,025 | 3,151 |
| Costs and Expenses | | | | | |
| Cost of income from rent, management and maintenance fees | 123 | 129 | 147 | 144 | 543 |
| Cost of income from sales, work and services | 139 | 113 | 107 | 141 | 500 |
| Sale and marketing | 47 | 50 | 47 | 56 | 200 |
| General and administrative | 32 | 29 | 26 | 36 | 123 |
| Portion of results of included companies, net of tax | 1 | 1 | 3 | 1 | 6 |
| Financing expenses | 31 | 105 | 53 | 69 | 258 |
| Other | - | 3 | 1 | 3 | 7 |
| Total Costs and Expenses | 373 | 430 | 384 | 450 | 1,637 |
| Profit before tax on income | 327 | 280 | 332 | 575 | 1,514 |
| Tax on income | (68) | (42) | (68) | (115) | (293) |
| Income from continuing operations | 259 | 238 | 264 | 460 | 1,221 |
| Loss from discontinued operations (after tax) | - | (2) | - | - | (2) |
| Net profit per period | 259 | 236 | 264 | 460 | 1,219 |
| Attributed to: | | | | | |
| Owners of the Company | 259 | 236 | 264 | 459 | 1,218 |
| Non-controlling interests | - | - | - | 1 | 1 |
| | 259 | 236 | 264 | 460 | 1,219 |

# Regulation 10C - Use of Proceeds from Securities

## Series D Bonds

On January 31, 2018, approx. NIS 1,367 million par value of Series D Bonds were issued in consideration for approx. NIS 1,409 million (approx. NIS 1,400 million net of attribution of the issue expenses), by way of expansion of the Series D Bonds of the Company in accordance with a shelf offering report released on January 31, 2018 (Ref. No.: 2018-01-010993), included herein by way of reference and released by virtue of a shelf prospectus.

## Series E Bonds

On January 22, 2019, approx. NIS 1,216 million par value of new Series E Bonds were issued in consideration for approx. NIS 1,216 million (approx. NIS 1,207 million net of attribution of the issue expenses), in accordance with a shelf offering report released on January 20, 2019 (Ref. No.: 2019-01-006388), included herein by way of reference and released by virtue of a shelf prospectus.

## Series F Bonds

On January 22, 2019, approx. NIS 263 million par value of new Series F Bonds were issued in consideration for approx. NIS 263 million (approx. NIS 260 million net of attribution of the issue expenses), in accordance with a shelf offering report released on January 20, 2019 (Ref. No.: 2019-01-006388), included herein by way of reference and released by virtue of a shelf prospectus.

The proceeds received from these issues were and shall be used by the Company, *inter alia*, for the refinancing of an existing financial debt and for current financing needs, from time to time, according to the Company's goals and business plans.

# Regulation 11 - List of Investments in Material Subsidiaries and Affiliates as of the Date of the Statement of Financial Position

See Annex A to this chapter.

# Regulation 12 - Changes in Investments in Material Subsidiaries and Affiliates, Directly and Indirectly, in the Report Period

In July 2018, the Company completed, through an (indirect) wholly owned American corporation, the purchase of an office building in Austin, Texas, U.S.A. For further details see Section 10.9 of Chapter A of this report.

| Date of Change | Nature of Change | Name of Company | Name of Holder | Remarks |
|---|---|---|---|---|
| July 2018 | Establishment of a new partnership for the purchase of a property | AG San clemente 3700, LLC | Azrieli Group Ltd. | See Section 10.9 of Chapter A of this report |

## Regulation 13 - Profit of Material Subsidiaries and Affiliates and the Corporation's Income therefrom as of the Date of the Statement of Financial Position (NIS in Million)

| Investee Company | Main Business | Profit (Loss) (NIS in million) | | Company's Income from the Affiliate | | |
|---|---|---|---|---|---|---|
| | | Net Profit | Comprehensive Income | Dividend | Management Fee | Interest and Linkage Differentials |
| Canit Hashalom Investments Ltd. | Development, management, construction, acquisition and lease of commercial and office buildings in Israel and in the US. Holding in Granite Hacarmel | 559 | 582 | - | - | 97 |
| Otzem Initiation & Investments (1991) Ltd. | Development, construction and lease of commercial buildings (Or Yehuda and Ramla) | 24 | 24 | - | - | 11 |
| AG Galleria Office Buildings, LP | Holding of 90% of the rights in office buildings situated in Houston, Texas, USA, which are known by the name Galleria | (33) | (1) | - | 5 | - |
| Gemel Tesua Investments Ltd. | Development, management, construction, acquisition and lease of commercial and office buildings in Israel | 59 | 59 | - | - | - |
| Otzma & Co. Investments Maccabim Ltd. | Development, management, construction, acquisition and lease of office buildings in Israel | 8 | 8 | - | - | 2 |
| AG Plaza at Enclave | Holding of 100% of the rights in an office building in Houston, Texas, USA - "Houston Dow Center" | (1) | 18 | - | - | 16 |
| Granite Hacarmel Investments Ltd. | Private holding company which holds, inter alia, Supergas and GES | 72 | 80 | - | - | - |
| Supergas Israel Gas Distribution Company Ltd. | Marketing of energy substitutes | 61 | 70 | - | - | - |
| Palace America Senior Housing Company Ltd. | Operation of a senior home for nursing and recuperation | 34 | 34 | - | - | - |

| | | | | | | |
|---|---|---|---|---|---|---|
| Ahuzat Bayit Ra'anana – Senior Housing Ltd. | Operation of a senior home and a retail center | 21 | 21 | - | - | 11 |
| Modi'in Senior Housing Ltd. | Establishment and operation of a senior home | 55 | 55 | - | - | 2 |
| Azrieli E-Commerce Ltd. | The eCommerce segment | (51) | (51) | - | - | 2 |
| International Consultants (E-Consult) Ltd. | Development, construction and lease of offices and industrial buildings | 11 | 11 | - | - | 6 |
| AG 8 West Centre | Holding of 100% of the rights in an office building in Houston, Texas, USA | 4 | 13 | - | - | 12 |
| AG San Clemente | Holding of 100% of the rights in an office building in Houston, Texas, USA | 4 | 9 | - | - | 2 |
| AG Two Aspen | Was established for the purpose of holding 100% of the rights in an office building in Austin, Texas, USA | 4 | 11 | - | - | 6 |

* Including capital reserve.

# Regulation 20 - Trade on the Stock Exchange – Listed Securities / Trading Suspensions - Dates and Reasons

## a. Shares/Securities

On February 4, 2018, approx. NIS 1,367 million par value of Series D Bonds were listed on TASE by way of expansion of the Series D Bond series.

On January 24, 2019, trade commenced on TASE in the new series of Series E Bonds issued by the Company under the shelf offering report released on January 20, 2019 (Ref. No. 2019-01-006388), with a par value of approx. NIS 1,216 million.

On January 24, 2019, trade commenced on TASE in the new series of Series F Bonds issued by the Company under the shelf offering report released on January 20, 2019 (Ref. No. 2019-01-006388), with a par value of approx. NIS 263 million.

For further details, see Regulation 10C of this Chapter D.

## b. Trading Suspensions

During the Report Period, there was no suspension of trading in the securities issued by the Company.

# Regulation 21 - Payments to Senior Officers

For a specification of the compensation granted in the Report Period, as specified in Schedule 6 of the Securities Regulations (Periodic and Immediate Reports), 5730-1970, see Section 1 of Chapter E of this Report – Corporate Governance.

# Regulation 21A - Control of the Company

As of the Report Release Date, Azrieli Holdings Inc. ("Azrieli Holdings"), a private company incorporated under Canadian law, holds, directly and indirectly, through its holding of the entire share capital of Nadav Investments Inc. ("Nadav Investments"), a private company incorporated under Canadian law, which is the direct controlling shareholder of the Company, 55.62% of the share capital and 61.31%[1] of the voting rights of the Company *de facto* and on a fully-diluted basis. As the Company has been informed, Azrieli Holdings is controlled by Sharon Azrieli, Naomi Azrieli and Danna Azrieli, either directly or through Canadian holding corporations.

Until his death, in July 2014, Mr. David Azrieli OBM directly and indirectly held approx. 44.77% of the share capital of Azrieli Holdings and all of the voting rights in Azrieli Holdings (including the voting rights of his children's shares, which were held by him in trust). Following the passing of Mr. David Azrieli OBM, the shares of Azrieli Holdings that had been held by him and his shares in a Canadian holding corporation controlled by him ("David Holding Corporation") were transferred to his estate, and Sharon Azrieli, Naomi Azrieli and Danna Azrieli were appointed as the 3 directors of Azrieli Holdings and of Nadav Investments. As the Company has been informed, on April 13, 2015, shares of Mr. David Azrieli OBM in Azrieli Holdings and in David Holding Corporation were distributed from his estate. Following such distribution, each one of Sharon Azrieli, Naomi Azrieli and Danna Azrieli, holds, directly and through David Holding Corporation, approx. 27.24% of the capital

1 Which include all of the voting rights by virtue of the Contribution Shares. According to the Contribution Arrangement (as defined in Note 35C(7) to the Financial Statements), Azrieli Holdings granted Azrieli Foundation Israel, by way of contribution without consideration, 6,902,000 ordinary shares of the Company of par value NIS 0.1 each, which constitute approx. 5.69% of the Company's issued capital (the "Contribution Shares").

rights in Azrieli Holdings and approx. 33.13% of the voting rights in Azrieli Holdings, and together they hold approx. 81.73% of the capital rights in Azrieli Holdings and approx. 99.39% of the voting rights therein. The remainder of Azrieli Holdings' shares are mainly held by the Azrieli Foundation of Canada (an interested party in the Company), which, following the distribution of the estate, holds (indirectly, through a holding of shares of David Holding Corporation) 15.93% of Azrieli Holdings' shares, with no voting rights (which holding indirectly constitutes a holding of approx. 8.86% of the capital rights of the Company), in addition to and separately from its direct holding of 8.55% of the capital and voting rights in the Company. As the Company has been informed, on March 20, 2017, a shareholders' agreement (the "2017 Agreement") was signed between Sharon Azrieli, Naomi Azrieli and Danna Azrieli (by themselves and through companies controlled by them), the indirect controlling shareholders of the Company and directors thereof (the "Controlling Shareholders"). Additional parties to the 2017 Agreement are Azrieli Holdings, Nadav Investments and David Holding Corporation (the three "Holding Corporations"). The 2017 Agreement replaces and substitutes the former shareholders agreement made by the parties in November 2012 (the "2012 Agreement"), and it regulates the relations between the Controlling Shareholders, by themselves, and through the Holding Corporations, in respect of their rights in the Company. Similarly to the 2012 Agreement, the terms of the 2017 Agreement include agreements regarding the sale and transfer of shares in the Company and in the Holding Corporations, including a lock-up period, right of first refusal, right of first offer, co-sale right and an exclusion in connection with certain sales of shares (drip) on TASE. The 2017 Agreement further prescribes that the manner of use of the voting rights in the Company will be determined by the Controlling Shareholders (by a majority vote), provided however, that in respect of resolutions to appoint directors of the Company, each one of the Controlling Shareholders shall have the right to use the voting rights to appoint one director who will be determined by her, whereas the manner of use of the voting rights in the Company regarding resolutions to appoint additional directors, will be adopted by a majority vote. Together with the 2017 Agreement, another agreement was signed between all of the direct shareholders in Azrieli Holdings (including the controlling shareholders). Such additional agreement was required under Canadian law, in order to ensure that Azrieli Holdings is subject to part of the provisions of the 2017 Agreement. It is clarified, that the 2017 Agreement does not change the identity of the Company's controlling shareholders (including of Azrieli Holdings) nor their percentage holdings in the capital and in the voting rights in the Company, and that as of the Report Release Date, Sharon Azrieli, Naomi Azrieli and Danna Azrieli are the Company's controlling shareholders. For further details see the immediate report of March 21, 2017 (ref. no.: 2017-01-026388), which is included herein by way of reference.

## Regulation 22 - Transactions with the Controlling Shareholder

For details with respect to transactions with the controlling shareholder or in the approval of which the controlling shareholder has a personal interest, in which the Company or a corporation controlled thereby or an affiliate thereof engaged, see Section 2 of the Company's Corporate Governance Report, which is attached as Chapter E hereof.

## Regulation 24 - Holdings of Interested Parties and Senior Officers

For details regarding the holdings of interested parties and senior officers of the Company, see the immediate report regarding the holdings of interested parties and officers released by the Company on April 10, 2018 (Ref. No.: 2018-01-036073), which is included herein by way of reference.

## Regulation 24A - Authorized Capital, Issued Capital and Convertible Securities

As of December 31, 2018, the registered share capital of the Company is 127,501,500 ordinary shares par value NIS 0.1 each, and the issued share capital of the Company is 121,272,760 ordinary shares par value NIS 0.1 each.

## Regulation 24B - The Company's Shareholders' Register

| Shareholder's Name | Company | Address | Class of Shares | Quantity of Shares | Par value |
|---|---|---|---|---|---|
| Registration Co. of Bank Hapoalim Ltd. | 510356603 | 62 Yehuda Halevi, Tel Aviv | Ordinary par value NIS 0.1 | 121,272,760 | NIS 0.1 |

## Regulation 26 - Directors of the Corporation (as of the Report Date)

Below are personal and professional details with regard to the Company's directors:

| (1) | Director's Name: | Danna Azrieli, Active Chairman of the Board |
|---|---|---|
| | Identification number: | 321657744 |
| | Date of Birth: | June 3, 1967 |
| | Address for service of process: | Azrieli Center 1, Tel Aviv |
| | Citizenship: | Israeli |
| | Membership on board of directors' committees | None |
| | Outside Director/Independent Director: | No |
| | Position filled at the Company/Subsidiary/Affiliate of the Company or of an interested party therein: | Active Chairman of the Board |
| | Date of commencement of service as director of the Company: | June 1, 2010 |
| | Education: | BA in Sociology and Anthropology from Swarthmore College; Juris Doctor of Law from Vermont Law School; member of the Massachusetts State Bar Association in the U.S. and the Israel Bar Association. |
| | Occupation in the past five years and other corporations in which he holds office as director: | Active Vice Chairman of the Board of the Company; Serves as a director of the companies: Nadav Investments Inc., Azrieli Holdings Inc., Candan Residences Ltd., Dan Squared Ltd., Candan Constructions' Maintenance and Management Ltd., Candan Management Services Ltd. and Candan Holdings Ltd.; Chair of Azrieli Foundation (Israel), R.A., Director of Azrieli Foundation (Canada), a Canadian nonprofit organization, Director of Weizmann Institute of Science, Director of Tel Aviv University and Director of Darca Schools NPO (R.A.). |
| | Family relation to an interested party: | Controlling shareholder. For details see Regulation 21A above. |
| | Accounting and Financial Expertise or Professional Qualification: | Professional Qualification |

| (2) | Director's Name: | Sharon Azrieli |
|---|---|---|
| | Identification number: | HM841817 |
| | Date of Birth: | August 4, 1960 |
| | Address for service of process: | Azrieli Center 1, Tel Aviv |
| | Citizenship: | Canadian |
| | Membership on board of directors' committees | None |

| | | |
|---|---|---|
| | Outside Director/Independent Director: | No |
| | Position filled at the Company/Subsidiary/Affiliate of the Company or of an interested party therein: | None |
| | Date of commencement of service as director of the Company: | June 1, 2010 |
| | Education: | PhD in Music from the University of Montreal; MA in Music from the University of Montreal; BA in Art from Vassar College; Certificate from the Juilliard School of Music; Associate degree from the Parsons School of Design. |
| | Occupation in the past five years and other corporations in which he holds office as director: | Opera singer, cantor and artist;<br>Publisher of interior design magazines;<br>Member of the board of Azrieli Foundation (Israel), R.A., and director of Azrieli Foundation (Canada), a Canadian nonprofit organization.<br>Serves as President of the Directors Board of the Orchestre de Chambre McGill; Sharon Azrieli Foundation for the Arts (SAFA); Opera Cares Foundation; Shir Chadash Synagogue.<br>A director of the following organizations:<br>7809298 Canada Inc.; 7807872 Canada Inc.; Vancouver Home Magazine Inc.; Toronto Home Magazine Inc.; Montreal Home Magazine Inc.;<br>McCord Museum (Montreal); Canadian Vocal Arts Institute; America-Israel Cultural Foundation (AICF). My Dezign S.L Ltd.; Immeuble 348 Victoria Inc; Immeubles Avishar Inc; 4287690 Canada Inc; 6011667 Canada Inc.; Viva Diva Canada Inc.; Viva Diva U.S Inc.; Canbonim Ltd.; My Dezign Inc.; Canadian Children's Literacy Foundation.<br>Owner and manager of foreign private companies. |
| | Family relation to an interested party: | Controlling shareholder. For details see Regulation 21A above. |
| | Accounting and Financial Expertise or Professional Qualification: | No |
| (3) | Director's Name: | Naomi Azrieli |
| | Identification number: | HB510031 |
| | Date of Birth: | September 26, 1965 |
| | Address for service of process: | Azrieli Center 1, Tel Aviv |
| | Citizenship: | Canadian |
| | Membership on board of directors' committees | None |
| | Outside Director/Independent Director: | No |
| | Position filled at the Company/Subsidiary/Affiliate of the Company or of an interested party therein: | None |
| | Date of commencement of service as director of the Company: | June 1, 2010 |
| | Education: | PhD (D. Phil) in International History from Oxford University, England; Master of International Affairs in International Relations, Finance and Economics from Columbia University, New York; BA from the University of Pennsylvania in Political Science and Russian Studies. |
| | Occupation in the past five years and other corporations in which he holds office as director: | CEO and Director of the Azrieli Foundation (Canada), a Canadian nonprofit organization. Member of the board of Azrieli Foundation (Israel), R.A. Owner and manager of foreign private companies.<br>Director and president of the corporations: Canpro Investments Ltd., Omico Investments Ltd., Omico Residential Ltd.<br>Director in the following entities: Canadian Society for Yad Vashem, Technion International Board, Yeshiva University, Brain Canada Foundation, Weizmann Institute of Science. |

| | | |
|---|---|---|
| | Family relation to an interested party: | Controlling shareholder. For details see Regulation 21A above. |
| | Accounting and Financial Expertise or Professional Qualification: | Professional Qualification |
| (4) | **Director's Name:** | **Joseph Ciechanover** |
| | Identification number: | 5991468 |
| | Date of Birth: | October 1, 1933 |
| | Address for service of process: | Azrieli Center 1, Tel Aviv |
| | Citizenship: | Israeli |
| | Membership on board of directors' committees | Audit Committee, FSRC and Enforcement Committee |
| | Outside Director/Independent Director: | Independent Director |
| | Position filled at the Company/Subsidiary/Affiliate of the Company or of an interested party therein: | None |
| | Date of commencement of service as director of the Company: | May 6, 2010 |
| | Education: | PhD in Philosophy from Boston University; LLM from the Hebrew University; Completed his studies towards an MBA at the Hebrew University (missing final paper); LLM from the University of Berkeley California. |
| | Occupation in the past five years and other corporations in which he holds office as director: | Consultant for Etgar 2 Fund by way of the Atidim Funds Management Co. Ltd.<br>Director at Harel Investments, Insurance and Financial Services Ltd., Mifal HaPayis and a member of the board of directors at the Israel Museum.<br>Chairman and CEO of Atidim Funds Management Ltd., IYZ Investment Management Ltd. and J.C. Atara Ventures Ltd.<br>Member of the associations: the Jacob Isler Foundation, the Dayan Center – Tel Aviv University, the Elie Wiesel Foundation, RA and the Israel Science Foundation, the Clinical Genetics Society. Served as a director of Azrieli Foundation (Israel), R.A. |
| | Family relation to an interested party: | No |
| | Accounting and Financial Expertise or Professional Qualification: | Expert director; has accounting and financial expertise |
| (5) | **Director's Name:** | **Tzipora Carmon** |
| | Identification number: | 51528933 |
| | Date of Birth: | December 7, 1952 |
| | Address for service of process: | Azrieli Center 1, Tel Aviv |
| | Citizenship: | Israeli |
| | Membership on board of directors' committees | Audit Committee, Compensation Committee, FSRC and Enforcement Committee ("All of the Committees") |
| | Outside Director/Independent Director: | Independent |
| | Position filled at the Company/Subsidiary/Affiliate of the Company or of an interested party therein: | None |
| | Date of commencement of service as director of the Company: | May 19, 2013 |
| | Education: | BA in Sociology and Education, the Hebrew University, Jerusalem; MBA, UCLA, California, USA. |
| | Occupation in the past five years and other | Manager and owner of T.C. Exports Ltd. in the last 21 years; Director of |

| | | |
|---|---|---|
| | corporations in which he holds office as director: | Delta Galil Industries Ltd. and of Rafael – Advanced Defense Systems Ltd. |
| | Family relation to an interested party: | No |
| | Accounting and Financial Expertise or Professional Qualification: | Expert director; has accounting and financial expertise. |
| (6) | Director's Name: | Efraim Halevy, Outside Director |
| | Identification number: | 49871718 |
| | Date of Birth: | December 2, 1934 |
| | Address for service of process: | Azrieli Center 1, Tel Aviv |
| | Citizenship: | Israeli |
| | Membership on board of directors' committees | All of the Committees |
| | Outside Director/Independent Director: | Outside Director |
| | Position filled at the Company/Subsidiary/Affiliate of the Company or of an interested party therein: | None |
| | Date of commencement of service as director of the Company: | August 24, 2010 |
| | Education: | LL.M. - The Hebrew University in Jerusalem. Management studies of process leadership for senior executives –the Tel Aviv University. |
| | Occupation in the past five years and other corporations in which he holds office as director: | Member of the Executive Committee of the Hebrew University of Jerusalem |
| | Family relation to an interested party: | No |
| | Accounting and Financial Expertise or Professional Qualification: | Professional qualifications. |
| (7) | Director's Name: | Niv Ahituv, Outside Director |
| | Identification number: | 008115693 |
| | Date of Birth: | August 16, 1943 |
| | Address for service of process: | Azrieli Center 1, Tel Aviv |
| | Citizenship: | Israeli and Canadian |
| | Membership on board of directors' committees | All of the Committees |
| | Outside Director/Independent Director: | Outside Director |
| | Position filled at the Company/Subsidiary/Affiliate of the Company or of an interested party therein: | None |
| | Date of commencement of service as director of the Company: | August 24, 2010 |
| | Education: | BA in Mathematics and Physics from the Hebrew University.<br>MBA from Tel Aviv University<br>MA in Information Systems from Tel Aviv University.<br>PhD in Management (specialization in Information Systems) from Tel Aviv University. |
| | Occupation in the past five years and other corporations in which he holds office as director: | Dean of the Faculty for HiTech Studies, the Academic Studies Center; Professor Emeritus of the Faculty of Management at Tel Aviv University; Member of the management at Beit Lessin Theatre; member of the management of Keshet Eilon; Member of the "Profit-Sharing" Investments Committee at Migdal Insurance; Outside Director of Rapac Communication |

| | | |
|---|---|---|
| | | & Infrastructure Ltd.; Outside Director of Discount Investments; Chairman of the managing committee at the Hillel Association. |
| | Family relation to an interested party: | No |
| | Accounting and Financial Expertise or Professional Qualification: | Expert director; has accounting and financial expertise |

| (8) | Director's Name: | Oran Dror |
|---|---|---|
| | Identification number: | 024973315 |
| | Date of Birth: | August 2, 1970 |
| | Address for service of process: | Azrieli Center 1, Tel Aviv |
| | Citizenship: | Israeli |
| | Membership on board of directors' committees | Audit Committee, FSRC and Enforcement Committee |
| | Outside Director/Independent Director: | Independent Director |
| | Position filled at the Company/Subsidiary/Affiliate of the Company or of an interested party therein: | None |
| | Date of commencement of service as director of the Company: | November 18, 2014 |
| | Education: | BA in Economics and East Asian Studies from the Hebrew University, Jerusalem. Research studies in the field of management and marketing for two years at the Waseda University, Tokyo, Japan – School of Commerce. |
| | Occupation in the past five years and other corporations in which he holds office as director: | CEO and director of Axilion Ltd.; CEO and director of Dror Liat Investment Ltd. (a company he controls); executive director and VP Telecom – MEA Regional Management of Microsoft International; executive director and VP Sales at Microsoft Israel; CEO and director at N.B.X. – E - Service Solutions Ltd. (a company he controls); VP at Vatbox Ltd. (through Dror Liat Investment Ltd.). |
| | Family relation to an interested party: | Fourth degree cousin of the controlling shareholders and directors Danna, Sharon and Naomi Azrieli. |
| | Accounting and Financial Expertise or Professional Qualification: | Expert director; has accounting and financial expertise |

| (9) | Director's Name: | Menachem Einan |
|---|---|---|
| | Identification number: | 008995383 |
| | Date of Birth: | June 17, 1939 |
| | Address for service of process: | Azrieli Center 1, Tel Aviv |
| | Citizenship: | Israeli |
| | Membership on board of directors' committees | Audit Committee, FSRC and Enforcement Committee |
| | Outside Director/Independent Director: | No |
| | Position filled at the Company/Subsidiary/Affiliate of the Company or of an interested party therein: | In addition to his being a director of the Company, Mr. Einan served as an external consultant of the Company until February 28, 2017. |

| | |
|---|---|
| Date of commencement of service as a director of the Company: | March 22, 2016 |
| Education: | BA in Humanities from Tel Aviv University; degree in Business Administration from UCLA. |
| Occupation in the past five years and other corporations in which he holds office as director: | Director and Active Deputy Chairman of the Board of the Company until February 2015;<br>Served as Chairman of the Board of Granite Hacarmel Investments Ltd. and as a director at Tambour Ltd., Sonol Israel Ltd., Supergas Israel Gas Distribution Company. Ltd. and GES Global Environmental Solutions Co. Ltd. until February 2015. A director of Leumi Card Ltd., member of the board of Azrieli Foundation (Israel), R.A. |
| Family relation to an interested party: | No |
| Accounting and Financial Expertise or Professional Qualification: | Professional qualifications |

## Regulation 26A: Senior Officers of the Corporation as of the Report Release Date

| Name | Eyal Henkin | Irit Sekler-Pilosof | Arnon Toren | Gideon Avrami | Ran Tal | Israel Keren | Avraham Jacoby | Moshe Cohen | Rafi Wunsh | Sharon Arie | Yoram Polak Ben Porat | Rachel Mittelman | Assaf Aviv |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Identity Number | 024604332 | 025710542 | 054121678 | 56524325 | 027474824 | 003105657 | 052253747 | 051209971 | 028145738 | 023544612 | 056000813 | 035730746 | 31787625 |
| Date of Birth | November 3, 1969 | October 31, 1973 | July 14, 1957 | July 6 1960 | May 22, 1974 | September 17, 1947 | March 31, 1954 | April 3, 1952 | February 15, 1971 | July 2, 1968 | July 29, 1959 | August 14, 1978 | August 12, 1974 |
| Office Commence-ment Date | January 1, 2018 | May 1, 2013 | November 1, 2013 | May 15, 2016 | August 1, 2016 | July 1, 2002 | July 1, 1987 | March 22, 2017 | October 15, 2010 | December 1, 2017 | March 22, 2016 | September 1, 2018 | March 1, 2019 |
| Position held in the Company/ Subsidiary/ Affiliate or in an interested party | CEO of the Company. CEO of Canit Hashalom Investments Ltd. Chairman of the Board of Directors of Granite Hacarmel, and subsidiaries thereof from January 1, 2018 (in lieu of Mr. Yuval Bronstein whose office ended). Director in Azrieli E-Commerce Ltd. | CFO and in charge of financial risks at the Company, and a director of Mini Israel and of SONAPCO | Deputy CEO and Head of Malls. Director in Azrieli E-Commerce Ltd. | VP, Head of Office Segment | VP, General Counsel and Company Secretary | CEO of asset companies Gemel Tesua Investments Ltd., Otzma & Co. Investments-Maccabim Ltd., Urban A.A.R. Ltd., Azrieli Ra'anana and Herzliya Business Park Operations Ltd. | Chief Comptroller, Azrieli Group Ltd. | The internal auditor | VP International Real Estate | VP Engineering and Construction | VP, Head of Senior Housing Sector | Chief Information Officer | VP Innovation and Business Development |

| Name | Eyal Henkin | Irit Sekler-Pilosof | Arnon Toren | Gideon Avrami | Ran Tal | Israel Keren | Avraham Jacoby | Moshe Cohen | Rafi Wunsh | Sharon Arie | Yoram Polak Ben Porat | Rachel Mittelman | Assaf Aviv |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Education | B.A. in Computer Science and Management from Tel Aviv University; Executive MBA, in the Kellogg Recanati program of Northwestern University and Tel Aviv University | B.A. in Business Administration, major in Accounting, The College of Management; LL.M., Bar Ilan University; Licensed as a CPA (Israel) | B.A. in Economics and Sociology, Hebrew University | B.A. in History and International Relations, the Hebrew University 1986. Diploma in Hotel Management 1994. | LL.B from Haifa University; LL.M from the Hebrew University of Jerusalem | B.A. in General History, Tel Aviv University | B.A. in Accounting and Economics, Bar Ilan University; Licensed as a CPA (Israel) | CPA, B.A. in Economics and Accounting, Tel Aviv University | B.A. in Economics and Accounting, Hebrew University of Jerusalem | Technion graduate of studies of Civil Engineering | Technion graduate of studies of Business Administration and Hotel Management | Industrial and Management Engineer and an MBA both from Tel Aviv University | B.A. in Business Management and MBA, specializing in marketing from the College of Management |
| Business experience in the last five years | CEO of Supergas Israel Gas Distribution Company Ltd. in the eight years prior to his appointment as CEO | Comptroller in Azrieli Group in the 13 years preceding the office commencement date. | Manager of the office segment in Azrieli Group and CEO of Azrieli Center in Tel Aviv in the six years prior to his current appointment; Director of Vardinon Real Estate and Investments Ltd. | CEO of Azrieli Towers 2001-2004. CEO of Jerusalem mall, Malcha 2005-2016 | VP, General Counsel, Gilat Satellite Networks Ltd. VP, General Counsel, Netafim Ltd. | Manager of properties, property marketing and management of logistics projects | Managing comptroller, Azrieli Group | Managing partner at Chaikin Cohen Rubin & Co.; director and manager at private companies affiliated with Chaikin Cohen Rubin & Co., CPA; internal auditor at a large number of public companies and public entities | VP Quebec Region, Elad Group Canada Inc. CFO, Elad Group Canada Inc. | VP Engineering, Nitsba Holdings, VP Engineering and Business Development, Aura Israel | Head of Senior Housing Development at the Group for the past three years. Previously CEO and director of Hon, a real estate management company of the Property & Building Group and the CEO of the chain Mediterranean Towers – Senior Housing for 14 years. | Chief Information Officer Supergas Israeli Gas Distribution Company Ltd. | VP Marketing, Bezeq International |

None of the officers is an interested party in the Company or has a family relation to another officer of the Company or to another interested party in the Company.

## Senior officers whose office ended during the Report Period and in the subsequent period until the Report Date:

None of the senior officers at the Company ended their office during the Report Period and in the subsequent period until the Report Date.

## Regulation 26B – Authorized Signatories of the Corporation

See Section 8 of Chapter E of this Report - Corporate Governance.

## Regulation 27 - The Company's Accountants

The Company's auditors are Brightman Almagor Zohar & Co., CPA, 1 Azrieli Center, Tel Aviv.

## Regulation 28 – Changes in the Memorandum or Articles of Association

No change was performed in the Report period.

## Regulation 29 - Resolutions and Recommendations of the Board of Directors

See Section 4 of Chapter E of this Report - Corporate Governance.

## Regulation 29A - The Company's Resolutions

See Section 4 of Chapter E of this Report - Corporate Governance.

## Exemption, Indemnification and Insurance of Officers:

For a description of the applicable arrangements with regard to exemption, indemnification and insurance for Directors and Officers in the Company, see Note 35D to the Financial Statements as of December 31, 2018.

| | |
|---|---|
| Danna Azrieli,<br>Chairman of the Board of Directors | Eyal Henkin, CEO |

Date: March 19, 2019

## Annex A – Regulation 11 – List of Investments in Material Subsidiaries and Affiliates as of the Date of the Statement of the Financial Position

| | | | | Rate in % | | | NIS in million | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Company name | Shares' class | Total par value of shares in NIS | Total par value of held shares in NIS | Of the capital | Of voting | Authority to appoint Directors | Cost of the held shares | Book value of investment (*) | Balance of the loans from the Company | Manner of presentation in the financial statements | Company's country of incorporation | Securities exercisable into capital rights or voting rights in the Company's investee company | Guaranties the Company provided to the investee company |
| Directly held companies | | | | | | | | | | | | | |
| Canit Hashalom Investments Ltd. | ordinary | 114 | 114 | 100% | 100% | 100% | 51 | 8,504 | (1) 2,393 | Consolidated Company | Israel | - | - |
| International Consultants (Iconsult) Ltd. | ordinary | 3,900 | 3,900 | 100% | 100% | 100% | 30 | 94 | (2) 36 | Consolidated Company | Israel | - | |
| Otzem Initiation & Investments (1991) Ltd. | Management | 80 | 80 | | | 100% | - | 214 | (2) 344 | Consolidated Company | Israel | - | - |
| | ordinary A | 21,330,220 | 21,330,220 | | | | | | | | | | |
| | ordinary B | 4,999 | 4,999 | | | | | | | | | | |
| | | 21,335,299 | 21,335,299 | 100% | 100% | 100% | | | | | | | |
| Azrieli E-Commerce Ltd. | ordinary | 1,600 | 1,600 | 100% | 100% | 100% | 26 | (74) | (2) 126 | Consolidated Company | Israel | | |
| Modi'in Senior Housing | ordinary | 1,000 | 1,000 | 100% | 100% | 100% | 32 | 101 | (2) 31 | Consolidated Company | Israel | | |
| AG Galleria Office Buildings, LP (3) | | - | - | 100% | 100% | - | 188 | 113 | - | Consolidated Company | USA | - | Guarantee in several cases which were defined in the loan agreement |
| AG Plaza at Enclave (3) | | - | - | 100% | 100% | - | 53 | 137 | 89 | Consolidated Company | USA | - | Guarantee in several cases which were defined in the loan agreement |
| AG 8 West Center (3) | | - | - | 100% | 100% | - | 19 | 38 | 66 | Consolidated Company | USA | - | Guarantee in several cases which were defined in the loan agreement |
| AG San Clemente (3) | | | | 100% | 100% | - | 88 | 73 | (4) 72 | Consolidated Company | USA | | Guarantee in several cases which were defined in the loan agreement |
| AG Two Aspen (3) | | - | - | 100% | 100% | - | 23 | 48 | 45 | Consolidated Company | USA | - | Guarantee in several cases which were |

| | | | | | | | | | | | | defined in the loan agreement |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Companies held by Canit Hashalom** | | | | | | | | | | | | |
| Granite Hacarmel Investments Ltd. | ordinary | 147,146,834 | 147,146,834 | 100% | 100% | 100% | 1,059 | - | Consolidated Company | Israel | - | - |
| | | | | | | | | | | | | |
| Gemel Tesua Investments Ltd. | ordinary | 53,750,000 | 53,721,650 | 99.9% | 99.9% | | - | - | Consolidated Company | Israel | - | - |
| Otzma & Co. Investments Maccabim Ltd. | ordinary | 16,100,000 | 16,091,764 | 99.9% | 99.9% | 100% | - | (2)88 | Consolidated Company | Israel | - | - |
| **Companies held by Palace Senior Housing Group Ltd.** | | | | | | | | | | | | |
| Palace America Senior Housing Company Ltd. | ordinary | 100 | 100 | 100% | 100% | 100% | 270 | - | Consolidated Company | Israel | - | - |
| Ahuzat Bayit Ra'anana Senior Housing Ltd. | ordinary | 15,000,000 | 15,000,000 | 100% | 100% | 100% | 55 | (2)459 | Consolidated Company | Israel | - | - |
| **Companies held by Granit HaCarmel Investments Ltd.** | | | | | | | | | | | | |
| GES Global Environmental Solutions Ltd. | ordinary | 17,304,169 | 17,304,169 | 100% | 100% | 100% | 57 | - | Consolidated Company | Israel | - | See Note 29B(7) |
| Supergas Israel Gas Distribution Co. Ltd. | ordinary | 252 | 252 | 100% | 100% | 100% | 32 | - | Consolidated Company | Israel | - | - |

* The data refers solely to the companies directly held by the Company.

(1) After deduction of capital reserve

(2) Capital notes after deduction of capital reserve

(3) Foreign partnership

(4) Including loan and capital notes after deduction of capital reserve

# Corporate Governance

# Part E

# CHAPTER E – CORPORATE GOVERNANCE REPORT

# PART A | ASPECTS OF CORPORATE GOVERNANCE

Following are details regarding corporate governance processes in the Company for 2018, which include both issues relating to corporate governance in accordance with the Securities Regulations (Periodic and Immediate Reports), 5730-1970 (the “Report Regulations”), and a corporate governance questionnaire in accordance with the version included in the document on proposed legislative amendments regarding improvement of the reports which was published by the Israel Securities Authority on March 16, 2014.

## 1. Regulation 21 - Payments to Interested Parties and Senior Officers – 2018

The compensation as recognized in the Company’s financial statements in 2018 for the five highest paid individuals among the senior officers of the corporation or a corporation controlled thereby, in connection with their office at the corporation or a corporation controlled thereby, are as follows (in terms of annual costs to the corporation, NIS in thousands, for the twelve-month period that ended on December 31, 2018 (as specified in the Sixth Schedule of the Reports Regulations):

| Details of the Compensation Recipient | | | | Compensation | | | |
|---|---|---|---|---|---|---|---|
| Name | Position | Position Scope | Rate of Holding in the Corporation's Capital | Management Fee (a) | Bonus | Other | Total |
| (1) Danna Azrieli | Active Chairman of the Board | 100%* | (b) | 2,911 | 1,500 | - | 4,411 |
| (2) Eyal Henkin | CEO of the Company | 100% | --- | 3,879 | 954 | 1,747(c) | 6,580 |
| (3) Arnon Toren | Deputy CEO and Head of Malls Segment | 100% | --- | 3,148 | 760 | - | 3,908 |
| (4) Irit Sekler-Pilosof | CFO | 100% | --- | 2,205 | 536 | - | 2,741 |
| (5) Gideon Avrami | VP Head of Offices | 100% | --- | 1,721 | 275 | 5(c) | 2,001 |

* It is clarified that Ms. Danna Azrieli may continue to perform additional activities, including philanthropic activities in which she is involved, from time to time, provided that performance thereof does not compromise the fulfillment of her duties at the Company.

a)The management fee component includes the following components: cost of monthly management fees and/or cost of monthly salary, social rights, social and related benefits as customary, car maintenance and reimbursement of communication and other expenses.

b) For details regarding control of the Company on the Report Date see Regulation 21A of Chapter D of the Report.

c) Reflects expenses in 2018 due to adjustment.

## (1) Ms. Danna Azrieli

Ms. Danna Azrieli has been serving as the Company's Active Chairman of the Board since July 2014. For details with respect to the management agreement of Ms. Danna Azrieli, which took effect on January 1, 2015, see Note 35C(1) to the financial statements. On October 6, 2016, the general meeting of the Company's shareholders (after the approval of the Compensation Committee and the Board of Directors of the Company on August 22, 2016 and August 24, 2016, respectively) approved extension of the said management agreement of Ms. Danna Azrieli as chairman of the Company's Board for another three years from the date of the meeting's approval as aforesaid (ref. no.: 2016-01-060735). It is emphasized that there is no change in the terms and conditions of the agreement which was approved in October 2016 versus the agreement that was approved in December 2014. The reports mentioned in this Paragraph (1) are included herein by way of reference.

According to the provisions of the Company's compensation policy[1] (the "Compensation Policy"), the Chairman of the Board is entitled to an annual bonus for meeting an adjusted profit target[2]. In 2018, the adjusted profit was approx. NIS 1,258 million, and therefore the sum of the variable bonus to which Ms. Danna Azrieli is entitled for the 2018 results was NIS 1,500 thousand.

## (2) Mr. Eyal Henkin

Mr. Henkin holds office as the Company's CEO since January 1, 2018, through a company that he owns. Prior thereto, starting from September 1, 2010 and until December 31, 2017, Mr. Henkin held office through a company owned by him as the CEO of Supergas (after previously serving as Deputy CEO of Supergas for approx. eight months). In consideration for his office as the Company's CEO, Mr. Henkin is entitled to fixed monthly management fees in a sum of NIS 313,000, linked to the rate of the rise in the Consumer Price Index for June 2016 as published in July 2016 (the date of publishing the rate of the index determined in the Compensation Policy). In addition, he is entitled to a 9-month adjustment period and in any event of termination of the Agreement, the Company shall pay Mr. Henkin, for the adjustment period, the full consideration and ancillary benefits. In addition, Mr. Henkin was granted a letter of indemnification and exemption in accordance with the Compensation Policy and as customary for the Company's other officers (who are not directors and controlling shareholders), and included in the insurance policy of the Company's officers[3]. Additionally, the Company shall provide Mr. Henkin with a suitable Grade 7 car and the Company shall bear the full cost of the car's use. The Company shall indemnify Mr. Henkin (including the management company through which he provides the CEO's services as aforesaid), as customary for such positions, for the actual expenses occasioned to him in providing the CEO's services to the Company, all in accordance with the Company's procedures and against the presentation of suitable references. The reimbursement of expenses as aforesaid shall not be more than the maximum amount determined, from time to time, by the Compensation Committee, that it determines is

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1 The Company's compensation policy that was amended and approved by the Company's general meeting on October 6, 2016. For details see Section 3 of the notice of meeting report as published on August 28, 2016 (Ref.: 2016-01-111643), included herein by way of reference.

2 "The Adjusted Profit for the Chairman" for this purpose, in respect of each calendar year – annual pre-tax profit, in accordance with the audited consolidated annual financial statements of the Company, net of the following amounts: (1) a dividend that it received from financial assets available for sale which was included in the annual pre-tax profit; (2) profit (loss) deriving from revaluation of real properties; (3) results of companies which do not engage in the core segments (real estate) of the Company and were included in the annual pre-tax profit; (4) linkage differentials accrued on financial liabilities; (5) interest expenses at the actual weighted effective interest rate for such year, of the Company and companies controlled thereby which engage in the Company's core business, in respect of loans (regardless of whether or not they were taken), at a financing rate of 65% on the historic purchase cost on the books of the investment in companies which are not in the core business; (6) the sum total of management fees (including bonus) for the (active) Chairman of the Board for such year, as included in the annual pre-tax profit; and (7) profit (loss) from financial assets (marketable securities) held for trading, including any interest and dividend in respect thereof.

3 For details about the letters of indemnity and exemption that the Company grants the officers as at the date of this Report, see Section 6 of the meeting notice report of March 23, 2017 (Ref.: 2017-01-028392), which is included herein by way of reference.

appropriate, having regard to the Company's activity and scope. In addition, the Company shall provide him with a mobile phone and bear its full cost and the cost of use thereof. Each one of the parties may bring the Agreement to an end, for any reason, subject to the grant of written 3-month notice. In addition, according to the Company's Compensation Policy, Mr. Henkin will be entitled to an annual bonus, according to the following criteria: first criterion – measurement of the officer's contribution – the Compensation Committee and the Board of Directors will examine (after receipt of the recommendation of the chairman of the Company's board) the CEO's meeting of criteria that shall mainly be based on the CEO's contribution to the Company in accordance with his duties and responsibilities; second criterion – amount of the bonus – upon fulfillment of the aforesaid, the Compensation Committee and the Board of Directors will be entitled to decide, in relation to the CEO, on the granting of a bonus in an amount that shall not exceed the sum of up to three times the monthly payment.

In accordance with the aforesaid, on March 17, 2019, the Compensation Committee examined, and on March 19, 2019 the Company's Board of Directors examined the CEO's contribution (after the recommendation of the Chairman of the Board was received), and it was resolved that on the basis of his contribution as aforesaid and the Company's results for 2018, Mr. Henkin will be granted a bonus in the sum of three (3) times the monthly management fees.

### (3) Mr. Arnon Toren

As of June 1, 2014, Mr. Toren holds the office of Deputy CEO of Azrieli Group and Head of the Mall Segment (following his former office as CEO of Azrieli Malls), through a company he owns. In consideration for his services, Mr. Toren is entitled to index linked, fixed, monthly management fees which, as of December 31, 2018, amounted to approx. NIS 253 thousand and standard related benefits, including the provision of a (Grade 6) vehicle, cellular telephones, expense reimbursements and advance notice of 6 months. The Company bears the full cost of all the benefits (including the cost of use and gross-up of the tax value).

According to the Compensation Policy, an officer who does not serve as the CEO of the Company or as a director thereof will be entitled to an annual bonus in accordance with the following criteria: first criterion – measurement of the officer's contribution – the Chairman of the Board and the CEO of the Company will examine the officer's meeting of criteria that shall mainly be based on the officer's contribution to the Company in accordance with his position and responsibilities.

Second criterion – amount of the bonus – upon fulfillment of the aforesaid, the Chairman of the Board and the CEO will be entitled to decide on the granting of an annual bonus, if it is decided to grant the same, in an amount that shall not exceed a sum of up to three times the monthly cost of employment of such officer.

In accordance with the aforesaid, it was resolved to grant Mr. Toren a bonus in the sum of NIS 760 thousand for 2018.

### (4) Ms. Irit Sekler-Pilosof

Ms. Irit Sekler-Pilosof has been serving as the Company's CFO since May 1, 2013. For her work, Ms. Sekler-Pilosof is entitled to a gross fixed index-linked monthly salary which, as of December 31, 2018, amounts to approx. NIS 178 thousand, and standard related benefits, including the provision of a (Grade 6) vehicle, cellular telephones, expense reimbursements and advance notice of 6 months. The Company bears the full cost of all the benefits (including the cost of use and gross-up of the tax value). In accordance with the provisions of Section (3) above, it was resolved to grant Ms. Sekler-Pilosof a bonus in the sum of NIS 536 thousand for 2018.

## (5) Mr. Gideon Avrami

Mr. Gideon Avrami has been serving as the Company's VP Head of Offices since June 1, 2016. For his work, Mr. Gideon Avrami is entitled to a gross fixed index-linked monthly salary which, as of December 31, 2018, amounts to approx. NIS 92 thousand, and standard related benefits, including the provision of a (Grade 6) vehicle, cellular telephones, expense reimbursements, advance notice of 6 months and a 3-month adjustment period. The Company bears the full cost of all the benefits (including the cost of use and gross-up of the tax value). In accordance with the provisions of Section (3) above, it was resolved to grant Mr. Avrami a bonus in the sum of NIS 275 thousand for 2018.

The compensation which was paid during the year prior to the Report Release Date to interested parties in the Company who are not listed in the table above, in relation to services they provided as functionaries in the corporation or a corporation controlled thereby, are as follows (in terms of annual cost for the corporation, in NIS in thousand, for the period of the twelve months ended on December 31, 2018, as specified in the Sixth Schedule to the Reports Regulations):

| Name of compensation recipient | | | | Compensation | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| Name | Position | Scope of position | Rate of holding in corporation's capital | Salary | Bonus | Share-based payment | Management fee(*) | Other | Total |
| Eight directors | Directors of the Company (a) | --- | | --- | --- | --- | --- | 1,545 (b) | 1,545 |

a) Three independent directors, two outside directors, one dependent director and two directors who are controlling shareholders.
b) Directors' compensation.

## (6) Directors of the Company

In accordance with the Company's Compensation Policy, the compensation for outside directors and other directors of the Company who are not controlling shareholders of the Company and do not receive a salary or management fee as will hold office from time to time, shall be the compensation in the amount of the "maximum amount" per director, according to the rating of the Company as provided in the Companies Regulations (Rules on Compensation and Expenses for the Outside Director), 5760-2000 (the "Compensation Regulations") and the classification of such director. In addition, the directors may be included in an insurance policy for officers of the Company and shall receive an undertaking of indemnification, or indemnification pursuant to an indemnification permit and receive an exemption from liability subject to the provisions of the Companies Law. In 2018, the compensation paid by the Company to all of the independent directors (two outside directors and three independent directors), amounted to a total of approx. NIS 1,171 thousand and to the dependent director NIS 191 thousand. For further details, see Note 35C(9) and 35D to the financial statements. In addition, the directors are entitled to the reimbursement of expenses as accepted at the Company and in accordance with the Compensation Regulations.

Compensation of additional directors of the Company who are controlling shareholders: For details see Regulation 22 below – Compensation for additional directors who are controlling shareholders of the Company.

## 2. Regulation 22 - Controlling Shareholder Transactions

Following are details, to the Company's best knowledge, with regard to transactions with the controlling party or in the approval of which the controlling party has a personal interest, in which the Company or a corporation controlled by it or a company related to it engaged in the Report Period, and which are still in force as of the Report Date:

### Transactions listed in Section 270(4) of the Companies Law

- Engagement in a Management Agreement with a Management Company Controlled by Ms. Danna Azrieli

  As aforesaid, on December 28, 2014, the Company's general meeting approved the Company's engagement with a Company controlled by Ms. Danna Azrieli in a management agreement through which Ms. Danna Azrieli provides to the Company Active Chairman of the Board services. For details on the management agreement see Regulation 21(1) of this chapter above. On October 6, 2016, the general meeting of the Company's shareholders approved the extension of the management agreement, with no change to the terms and conditions of the engagement between Ms. Danna Azrieli and the Company, for another three years from the date of the meeting's approval (ref. no.: 2016-01-060735), which is included herein by way of reference, and see Note 35C(1) to the financial statements.

- Compensation of Additional Directors who are Controlling Shareholders of the Company

  Ms. Sharon Azrieli and Ms. Naomi Azrieli, controlling shareholders of the Company, are entitled to directors' compensation as approved by the Board and general meeting of the Company on May 6, 2010 and ratified by the Company's Board on May 13, 2013 and on May 24, 2016 (following receipt of the approvals of the Company's compensation committee) and reported to the public on May 14, 2013 and May 25, 2016, respectively, and pursuant to Section 1B(3) of the Companies Regulations (Relief in Transactions with Interested Parties), 5760-2000. The aforesaid compensation approval of May 25, 2016 was granted for a 3-year period commencing from June 3, 2016. In addition, the provisions of Sections 5(b) and 6(a) of the Compensation Regulations pertaining to reimbursement of expenses to directors, including flights, per diems and hospitality, shall apply also with regard to such directors, mutatis mutandis. The audit committee and board of directors approved a framework for such expenses, which is examined from time to time. In accordance with the aforesaid, in 2018, the compensation paid by the Company to Naomi Azrieli and Sharon Azrieli as aforesaid amounted to a total of approx. NIS 184 thousand. For details see immediate report published by the Company on May 25, 2016 (Ref. No.: 2016-01-033138), included herein by way of reference, Regulation 21(6) of this part above and Note 35C(9) to the financial statements.

- Insurance and Indemnification of Controlling Shareholders in the Company

  Ms. Danna Azrieli, Chairwoman of the Board of the Company, Ms. Naomi Azrieli, Director, and Ms. Sharon Azrieli, Director (the "Controlling Shareholders who are Directors"), are entitled to an officers' insurance arrangement to which all of the directors and officers of the Company are entitled. On May 30, 2018 the compensation committee approved an engagement for renewal of the insurance policy of the directors and officers of the Company (including among the controlling shareholders of the Company) and the Company's subsidiaries (other than with respect to Granite Hacarmel which holds an independent officers' insurance policy) from June 3, 2018 until June 2, 2019. The engagement is according to the framework of the engagement specified in the Company's Compensation Policy. In addition, the Controlling Shareholders who are Directors are entitled to letters of indemnification and exemption according to the Company's Compensation Policy. For details see Note 35D to the financial statements. On April 27, 2017 the Company's general meeting approved the amendment and extension of letters of indemnification that were granted to the Controlling Shareholders who are Directors, for an additional three year period, and the granting of exemption from liability to the Controlling Shareholders who are Directors, commencing from April 27,

2017. For further details see the notice of meeting report dated March 23, 2017 (Ref.: 2017-01-028392), and an immediate report on the results of the meeting dated April 20, 2017 (Ref.: 2017-01-043866), included herein by way of reference.

- Contributions to the Azrieli Foundation (Israel), a Registered Association

  In May 2010 (following approval by the board of directors), the general meeting, approved the Company's policy on contributions to the Azrieli Foundation (Israel) R.A. (the "Azrieli Foundation"). On March 14, 2013, the Company's audit committee determined that the length of time which was originally set forth by the general meeting of the Company in respect of the Company's contributions to the Azrieli Foundation, i.e. 5 years, is reasonable under the circumstances. In May 2015, the general meeting approved (after approval by the audit committee and board of directors of the Company) the Company's engagement with the Azrieli Foundation in a new contribution arrangement, whereby the arrangement for contribution to the Azrieli Foundation would be extended for an additional period of five years, commencing on June 1, 2015 and ending on May 31, 2020. For details about the contribution arrangement, see the invitation to a meeting report of April 16, 2015 (Ref. No. 2015-01-000186), which is included herein by way of reference, and Note 35C(7) to the financial statements. Sharon Azrieli, Naomi Azrieli and Danna Azrieli may be deemed as having a personal interest in the contribution to the Azrieli Foundation due to their office on the Company's Board and the Board of the Azrieli Foundation. It is further clarified that following the receipt of the contribution shares (for details with respect to the contribution shares, see Regulation 21A in Chapter D of the Report), the Foundation became an interested party in the Company, within the definition of such term in the Securities Law, and following the provisions of the aforesaid contribution arrangement, Azrieli Holdings and the Azrieli Foundation are deemed as "co-holders", within the definition of such term in the Securities Law; for the purpose of duties applicable or relating under the Companies Law to the controlling shareholders of the Company, the Company has chosen to treat the Azrieli Foundation as if it were a controlling shareholder of the Company, together with Azrieli Holdings, even if not required under the provisions of the law, and for as long as no other notice is given by the Company in an immediate report.

## Negligible Transactions

In the Report Period, the Group performed negligible transactions with the controlling parties thereof, or that the controlling parties thereof had an interest in their approval, of the kinds and characteristics in accordance with a negligible transactions procedure approved by the Board of Directors of the Company, as specified in Note 35E to the financial statements, including:

- Lease Agreements with Related Parties

  The Company, companies controlled by the Company and related companies thereof, have engaged in lease agreements with lessees, in the engagement with whom the controlling party has a personal interest, pursuant to which part of the aforesaid companies lease out for several years now and/or leased out during 2018, in the ordinary course of business and at market conditions, areas in some of the income producing properties of the Company. The income with respect to the aforesaid rentals in the year ending on December 31, 2018, totaled approx. NIS 1,593 thousand (about 4 lessees, including the Foundation). The Audit Committee and the Board of Directors of the Company examined in their meetings on March 17, 2019 and March 19, 2019, respectively, that these engagements, which were made during 2018, were negligible transactions which are carried out in the ordinary course of business of the Company and at market conditions. For details, see Note 35E to the financial statements.

  During the Report Period, a subsidiary of the Group employed one employee who is related to a controlling shareholder of the Company (and does not amount to the definition of "relative" in the Companies Law) in an employment agreement which is not irregular and is also negligible, in a total cumulative annual amount of approx. NIS 587 thousand.

- Ties with the community

  From time to time the Company makes, either itself or through companies which are among the members of the Group, direct contributions as well as contributions through the Foundation as specified in Section 2 above. In addition, to the Company's best understanding, the Foundation may donate to the community and to bodies or entities which require assistance, including bodies to which interested parties of the Company may have a link, or in which interested parties of the Company are volunteer members.

# 3. Additional Issues in Relation to the Control of the Company

## 3.1 Restructuring

In the context of a process of restructuring of the companies in the Group and primarily, steps for the consolidation of similar activities of the Group which were performed in fellow subsidiaries, and streamlining of the Group's current operation, the Company engaged, in November 2008, in an agreement with Nadav Investments whereby Nadav Investments transferred its shares in some of the Group's companies to the Company, as is, in consideration for an allotment of shares of the Company (the "Restructuring Agreement"). As of the Report Date, the restriction period by virtue of Section 104A of the Income Tax Ordinance (New Version), 5721-1961, pertaining to the sale of shares which have been transferred, has expired.

Due to it being a company which is incorporated under Canadian law, Nadav Investments is governed, *inter alia*, in connection with its operations or investments in Israel, by the rules of taxation which are set forth in the treaty between the State of Israel and Canada pertaining to the prevention of double taxation and tax evasion with regard to taxes on income and capital (the "Treaty"), including with regard to the sale of shares in companies whose assets are mainly real properties. For purposes of clarification and interpretation of the sections of the Treaty which contemplate this issue, various tax ramifications and provisions regarding the sale of the Company's shares were set forth in the context of an agreement between the Israel Tax Authority and the Company, Canit Hashalom and Nadav Investments, dated November 2008, in accordance with the rate of the Company's holdings in real properties in Israel.

In addition, the aforesaid agreement set forth provisions whereby Nadav Investments shall not act towards receiving any tax benefits in Canada which are not in accordance with the provisions of the law in Canada or the Treaty, provisions pertaining to the possibility to terminate the agreement if in the future the provisions of the Treaty and/or Chapter E of the Ordinance will be materially modified in the manner which has an effect on the manner of taxation of the sale, and additional provisions whereby in any event where there will be a tax liability in Canada due to the sale of the shares, the same shall have no effect on the tax liability which is set forth in the agreement. Any restructuring in accordance with the provisions of the second part of the Ordinance which addresses the Company's shares and/or the shares of Canit Hashalom shall be performed solely after the receipt of the advance consent of the Mergers and Splits Department of the Tax Authority.

## 3.2 Definition of Business

On May 24, 2016, the Company’s Board, after the approval of the Audit Committee of May 22, 2016, approved the Company’s Definition of Business Procedure (the “Procedure”) which shall apply to the Company’s directors and to the Company’s controlling shareholders. The Procedure determines the types of business in which they will not be able to engage in transactions in Israel and overseas, and the manner of disclosure to the Company, prior to engagement in such transactions, and the how the Company shall make the decision as to whether such transactions are relevant to the Company. The Procedure shall apply to controlling shareholders and board members at the Company and will be in effect throughout the period of their being controlling shareholders of the Company and/or their term of office as members of the Company's Board, whichever is later, and with respect to directors for an additional period of six months from the end of the said timeframe, so long as no other resolution shall have been adopted by the Company's Board, after receipt of the resolution of the Company's Audit Committee. The Procedure determines that a controlling shareholder and/or director of the Company is prohibited from being involved, either directly or indirectly, in business activity which may, according to the Companies Law, fall under the definition of a business opportunity of the Company, and in any event which falls within one or more of the activities to which the Procedure applies.

The Procedure regulates the process of approval of performance of the transaction by a controlling shareholder and/or director, if the Company chooses not to perform such transaction itself. According to the Procedure, a controlling shareholder and/or director is required to present, in writing, to the Company's management and subsequently to the Audit Committee, an outline of the transaction in connection with a property and/or activity which fall within any of the activities according to the Procedure which he is interested in performing, and to forward all of the material relevant to the transaction for their perusal. Only if the Company's management, and subsequently the Audit Committee, decide that the proposed activity does not interest the Company, will the controlling shareholder and/or director of the Company be free to engage in such transaction.

Due to the complexity of the issues covered by the Procedure, the timetables for performance of transactions and the concern of other bodies which may frustrate the transaction, decisions must be made under the Procedure on short notice and even immediately, all as specified in the Procedure. Therefore, the decision of the Audit Committee as to whether to approve the proposed activity or alternatively to seek supplementary details from the Company's management, shall be given no later than up to 10 business days after the date of presentation of the proposal by such person and receipt of the material and information required, such decision being made by a majority of members who do not have a personal interest in the decision.

It is clarified that the provisions of the Companies Law and the provisions of supplementary laws such as securities law prevail over the provisions of the Procedure, and therefore the Company is required to seek advice in each case according to the special circumstances thereof from the legal aspect, as applicable at such time.

In addition, there is a definition of business procedure for the Chairman of the Board, Ms. Danna Azrieli, which applies to her in addition to the provisions of the Procedure.

# 4. Regulation 29 and Regulation 29A - Recommendations and Resolutions of the Board of Directors

For details on resolutions of the board of directors with regards to dividend distributions see Section 4 of Chapter A of this Report and Notes 21 and 37A to the financial statements.

## Resolutions of the Special General Meeting

Set forth below is a specification of resolutions which were approved in special general meetings of the Company's shareholders:

| Date of resolution | Subject of resolution | Ref.[4] |
|---|---|---|
| April 30, 2018 | Approval of the terms of office and employment of Mr. Eyal Henkin as the Company's CEO (through a private company wholly owned by him). | 2018-01-043000 |

## Resolutions of the Company – Regulation 29A

In the Report Period, and until the Report Release Date, no Company resolutions were adopted on the issues specified in Regulation 29A of the Report Regulations, other than as specified below:

For details in relation to the resolution to renew the Company's insurance policy for directors and officers (including from among the controlling shareholders of the Company) of the Company and the Company's subsidiaries, with the exception of Granite Hacarmel Group which holds an independent officers' insurance policy, from June 2018 until June 2019 see Section 2 above, which is included in the specification with respect to insurance and indemnification for controlling shareholders of the Company, that was adopted pursuant to the provisions of Sections 1B(5) and 1B1 of the Companies Regulations (Relief in Transactions with Interested Parties), 5760-2000 and Note 35D to the financial statements.

# 5. Compensation of Senior Officers

The Company's Compensation Policy determines a compensation plan for officers of the Company, including directors of the Company who are controlling shareholders.

At the Compensation Committee's meeting of March 17, 2019 and at the board meeting of March 19, 2019, a discussion was held on the terms of employment and the compensation granted to the senior officers and the interested parties of the Company in 2018 which are specified in Regulation 21 of this chapter with respect to each one of the said senior officers and interested parties separately.

The Company's board of directors determined, after having received the recommendation of the compensation committee, *inter alia*, that all of the compensation terms of the officers are consistent with the Company's Compensation Policy.

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[4] The reports in this table are included herein by way of reference.

# 6. Internal Audit

In 2010 the Company adopted an internal audit procedure (the "Internal Audit Procedure"), whose purpose is to define the status and scope of activity of the internal auditing of the Company, as well as the methods and means for fulfillment of its tasks. This Procedure was approved by the audit committee in its meeting of November 15, 2010 and by the Company's board of directors in its meeting of November 24, 2010.

Identity of the Internal Auditor: Mr. Moshe Cohen, CPA and managing partner at Chaikin Cohen Rubin (the “Internal Auditor”), was appointed to the position of the internal auditor of the Company and the Group's companies (excluding Granite Hacarmel) and began his service at the Company in March 2017.

Compliance of the Internal Auditor with Legal Requirements: To the best of the knowledge of the Company's management, according to the Internal Auditor's statement, he complies with the requirements of Section 146 (b) of the Companies Law and the provisions of Section 3(a) and 8 of the Internal Audit Law, 5752-1992 (the "Internal Audit Law").

Holding Securities of the Company or a Body Related Thereto: As of this Report Date, as the Internal Auditor informed the Company, he does not hold securities of the Company or a body related thereto.

Ties of the Internal Auditor with the Company or a Body Related Thereto: To the best of the knowledge of the Company's management, as the Internal Auditor informed the Company, the Internal Auditor does not have material business or other ties with the Company, and nothing in other business ties of the Internal Auditor creates a conflict of interest with his duties as an Internal Auditor of the Company.

Additional Positions of the Internal Auditor in the Company: The internal auditor is an external service provider to the Company on behalf of Chaikin Cohen Rubin. According to the Internal Audit Procedure, the auditor and the audit workers will not hold a position in the Company in addition to the internal audit. As of the Report Date, except for his position as the Company's internal auditor, the internal auditor is neither employed by the Company nor provides any other external services thereto.

Other positions of the Internal Auditor outside the Company: Mr. Moshe Cohen is a managing partner at Chaikin Cohen Rubin.

Method of Appointment of the Internal Auditor: Mr. Moshe Cohen was appointed to serve as the internal auditor of the Company pursuant to the recommendation of the Company's audit committee of March 19, 2017 and the resolution of the Company’s board of directors of March 21, 2017, after an in-depth review of his education, qualifications and experience of many years in internal auditing while considering the obligations, authorities and duties imposed on the internal auditor according to law.

Mr. Cohen was found suitable to serve as the internal auditor of the Company, *inter alia,* considering the scope of business and complexity of the company. Within the framework of the Company’s Internal Audit Procedure which was approved by the audit committee and board of directors of the Company in November 2010, the Company's board of directors appointed the Internal Auditor and determined his status and compensation terms.

Conclusion of term of office: According to the Internal Audit Procedure which determines that the term of office of the Company’s internal auditor shall not exceed 6 years, and therefore on March 21, 2023 Mr. Moshe Cohen will end his term of office as the Company’s internal auditor.

The Identity of the Supervisor of the Internal Auditor: The organizational supervisor of the internal auditor is, as of the Report Date, the chairman of the Company's board of directors, in coordination with the Company's audit committee.

The Audit Plans: According to the Internal Audit Procedure, the internal auditor submits a proposal for an annual work plan, in coordination with the chairman of the board and the Company's CEO. The audit committee must discuss the plan and approve it, and thereafter the plan is forwarded for the board's approval. In November 2017, the audit committee adopted the report of the Internal Auditor regarding a multi-annual risk survey, according to which the audit committee laid down a multi-annual plan for the years 2017-2021 for determination of the audit objectives, which served as an outline for laying down the annual work plan of the internal audit. The audit plan of the internal auditor is an annual plan, derived from a multi-annual work plan, *inter alia*, according to the following considerations: potential for streamlining and saving, risks inherent to the Company's business, rules and regulations applicable to the Company and weaknesses which the Company's board of directors, management or internal auditor observe on an ongoing basis.

The annual work plan of the internal audit includes also the performance of an audit of the follow up on implementation of the internal auditor and audit committee's recommendations by the Company's management. The audit is carried out according to the plan under the supervision of the internal auditor and is adapted, according to developments and findings which are discovered during the audit. The work plan leaves discretion with the auditor for change in the audited issues, after a discussion on the subject with the relevant parties.

Material Transactions: The internal auditor receives an invitation, including background material for meetings of the Company's audit committee in which transactions are examined and approved, as specified in Section 270 of the Companies Law. According to his choice, after receiving proper details, he is present at the meetings or is updated in respect thereof. Also, the internal auditor may receive, according to his request, minutes of the Company's board meetings in which such transactions had been approved.

Audit of Investee Corporations: The internal auditor also serves as the internal auditor of the subsidiaries in the Group, excluding the Granite Hacarmel Group and the senior housing in which an internal audit is performed by other internal auditors. The audit plan also refers to material investee corporations of the Company in which no internal auditor had been appointed, including overseas.

Scope of Retaining of the Internal Auditor: The scope of retaining of the Internal Auditor was approved by the audit committee according to the audit plan which was approved thereby.

In respect of the audit plan for 2018, the hours of the internal audit in the Company and in its investee companies (excluding in Granite Hacarmel and senior housing) which were performed by the Internal Auditor amounted to approx. 1,143 hours. The management has the option to expand the scope of retaining according to circumstances.

In the Company's estimate, the scope of the Internal Auditor's work in respect of 2018 is appropriate.

The scope of hours for the audit work in the Company and in the subsidiaries is determined according to the audit plan proposed by the internal auditor and is approved by the audit committee.

In 2018, the internal audit hours in Granite Hacarmel Group amounted to approx. 358 working hours (which were performed by the EY accounting firm) and the internal audit hours in senior housing, which were performed by the Internal Auditor (CPA Gali Gana) amounted to approx. 185 working hours.

According to the Internal Audit Procedure, the period of office of an internal auditor in the Company will not exceed six years, unless the audit committee and the board of directors have decided otherwise.

Guideline Professional Standards in the Performance of the Audit: The internal auditor and the team of employees reporting to him perform the audit work in meticulous compliance with necessary standards for the performance of professional, reliable, autonomous audit, independent of the auditee. Pursuant to information provided to the Company's management by the internal auditor, the audit reports rely on the audit findings and the facts recorded in the audit are carried out according to accepted professional standards according to professional guidelines on internal auditing, including standards of the Institute of Internal Auditors in Israel (IIA), and in accordance with the Internal Audit Law, 5752-1992 and the Companies Law. The board of directors relied on the reports of the internal auditor regarding his compliance with the professional standards according to which he performs the audit.

Free Access to the Internal Auditor: The internal auditor of the Company has free, unlimited and direct access, in coordination, to documents, information and the relevant information systems of the Company, and of investee companies, including financial data, as well as an independent status. The internal auditor undertakes to keep in confidence, not to provide to others and not to make any use for his own use or for the use of others, of any information pertaining to the Company.

The Report of the Internal Auditor: The internal audit reports are submitted in writing and discussed on an ongoing basis with the Company's management and the CEO.

The dates on which a report was submitted regarding the findings of the Internal Auditor to the CEO are: on March 12, 2018 (2 reports) and on November 4, 2018 (one report and one risk survey). The dates on which a discussion was held at the audit committee on the findings of the Internal Auditor, are as follows: on March 18, 2018 (two reports), on November 18, 2018 (one report and one risk survey) and on March 17, 2019 (3 reports).

The Evaluation by the Company's Board of Directors of the Activity of the Internal Auditor: According to the evaluation of the board of directors, the qualifications of the internal auditor and his team, the scope, nature and continuity of the activity of the internal auditor and his work plan are reasonable in the circumstances of the matter, and fulfill the purposes of the internal audit at the Company.

On March 17, 2019, the chairman of the audit committee held a conversation with the internal auditor of the Company, in the absence of the Company's management, for discussion of the internal auditor's work and found that there are no restrictions on his work, as aforesaid.

Compensation of the Internal Auditor: The payment to the Internal Auditor of the Company and of subsidiaries in Israel is done according to actual working hours and according to the work plan approved by the audit committee and the progress in the audit work of each and every subject. In the beginning of each year the Internal Auditor submits a proposal for an annual audit plan which will include a planned hourly framework.

The audit committee determines the audit plan and the hour quota. The Internal Auditor will not deviate from the hour quota without the approval of the audit committee. In case that further tasks will be imposed on the Internal Auditor during the audit year – the audit committee will determine the hour quota for the further tasks.

In respect of 2018, the cost of the fee to the Internal Auditor and his team amounted to approx. NIS 240 thousand (plus VAT).

According to the Company's estimation, due to the fact that the remuneration is based on working hours, the aforesaid remuneration cannot affect the exercise of the internal auditor's professional discretion. The Company determined as a matter of essential policy the independence of the internal audit, and therefore, the internal auditor is not dependent at all upon the Company and the management thereof.

# 7. The Outside Auditor

## The Auditor's Identity

The primary outside auditors of the Company and of the investee companies (excluding some of the companies in the Granite Hacarmel group) are the accounting firm of Brightman Almagor Zohar (the "Auditor"). It shall be stated that the firm leases offices from the Company at the Azrieli Center in Tel Aviv for amounts which are immaterial to the Company. However, in order to ensure the independence thereof is not prejudiced, the Auditor has assumed (within the framework of an agreement with the Israel Securities Authority) parameters which will be examined from time to time in respect of the engagement, including with respect to the specificity of the terms of the lease agreement and non-modification thereof; written – at arm's length fee agreements; separation between the identity of the service providers and the decision makers in respect of the lease agreement; restrictions regarding the settling of accounts between the lease agreement and the services and agreement that in case of dispute the auditor shall act for termination of his office. The Company confirms with the Auditor the fulfillment of such parameters and the validity thereof on an annual basis.

## The Auditor's Fee

In the years 2017 and 2018, the accountant fee for audit services, audit-related services and tax services and consultation services totaled as follows:

| 2018 | | Audit Services, Audit-Related Services and Tax Services | | Other Services | | Total | |
|---|---|---|---|---|---|---|---|
| Company | Auditor | NIS in thousands | Hours | NIS in thousands | Hours | NIS in thousands | Hours |
| Azrieli Group Ltd. | Brightman Almagor Zohar & Co., CPAs | 2,000 | 9,110 | 60 | 155 | 2,060 | 9,265 |
| Supergas and GES | Somekh Chaikin KPMG (auditors) | 568 | 3,530 | 182 | 480 | 750 | 4,010 |

| 2017 | | Audit Services, Audit-Related Services and Tax Services | | Other Services | | Total | |
|---|---|---|---|---|---|---|---|
| Company | Auditor | NIS in thousands | Hours | NIS in thousands | Hours | NIS in thousands | Hours |
| Azrieli Group Ltd. | Brightman Almagor Zohar & Co., CPAs | 1,915 | 8,767 | 96 | 284 | 2,011 | 9,051 |
| Supergas and GES | Somekh Chaikin KPMG (auditors) | 557 | 3,465 | 287 | 790 | 844 | 4,255 |

## Determination of the Auditor's Fee

The Company's board of directors, after receiving the recommendation of the Company's audit committee, was authorized in the Company's articles of association to determine the fee of the outside auditor. The fee is determined based on the work required and past experience, while adjusting such to changes in regulation and scope of work, development of the Company and events which occurred during the passing year.

## 8. Independent Authorized Signatory

As of the Report Release Date, the Company does not have an independent authorized signatory.

## 9. Contributions

The Company has a deep commitment to the improvement and promotion of the community in Israel. The social accountability, the integration and giving to the community are strategic objectives which constitute an integral part of the Company's business work plan, which allocates financial resources to the matter, in the annual work plan, mainly under the contribution arrangement, as specified in Section 2 of this chapter.

Over the course of 2018 the Company made contributions, itself and through consolidated companies (excluding Granite Carmel), in money and in finished products, at a total value of approx. NIS 14.1 million.

For resolutions adopted by the Company in respect of its contribution policy, through the Azrieli Foundation (Israel), which also includes undertakings to grant future contributions, see Regulation 2 above and Note 35C(7) to the financial statements.

## 10. Internal Enforcement Plan in the Company

In 2012, the Company has adopted an internal enforcement plan. Within the framework of the internal enforcement plan, the Company's board of directors appointed a board committee designated for the issue of internal enforcement in the Company (the "Enforcement Committee") which held a series of discussions regarding required adjustments for an enforcement outline and an enforcement system procedure for the needs of the Company, the unique structure of the Company and its field of business. The supervisor of internal enforcement in the Company is Adv. Ran Tal, VP, General Counsel and Company Secretary.

In the context of the enforcement plan, the Company updated and adopted several procedures regarding corporate governance in the Company, which constitute part of the overall enforcement system in the Company, including: (a) Procedure for the work of the board and its committees; (b) Procedure for identifying transactions with related parties (which also addresses the identification of transactions with interested parties, the classification of irregular and negligible transactions and criteria for types of transactions and acts as being irregular); (c) Immediate reports procedure (for examination of the materiality and the need for submitting an immediate report upon the occurrence of various events); (d) Insider information procedure; (e) Whistleblower employees procedure; (f) Ethical code; (g) Officer holdings procedure; (h) Cluster of companies procedure; (j) Definition of business for directors and controlling shareholders of the Company procedure and other procedures designated to support and regulate the work of the different organs in the Company and its management.

In 2018, the Company implemented the enforcement plan and acted in accordance therewith, in the context of which it also held the annual training day, which compiles the relevant updates for the managers and employees of the Group. A report for 2018 and an enforcement plan for 2019 were deliberated by the Enforcement Committee on March 17, 2019.

# PART B | CORPORATE GOVERNANCE QUESTIONNAIRE[5]

To clarify, for the avoidance of doubt, the questionnaire is not intended to exhaust all corporate governance aspects relevant to the Company, but only addresses several aspects; for receipt of further information, please inspect the Company's reports, including in this periodic report.

## Independence of the Board of Directors

| | | Correct | Incorrect |
|---|---|---|---|
| 1. | Throughout the entire report year, two or more outside directors held office in the corporation.<br>In this question you may reply "Correct" if the period of time in which two outside directors did not hold office does not exceed 90 days, as provided in Section 363A(b)(10) of the Companies Law however, any reply which is (Correct/Incorrect) shall state the period (in days) in which two or more outside directors did not hold office in the corporation in the report year (including also a term of office which was retroactively approved, while distinguishing between the different outside directors):<br>Director A: Prof. Niv Ahituv<br>Director B: Mr. Efraim Halevy<br>Number of outside directors holding office in the corporation as of the date of release of this questionnaire: 2. | ✓ | |
| 2. | The rate[6] of independent directors[7] holding office in the corporation as of the date of release of this questionnaire: 5/9<br>The rate of independent directors determined in the articles of association[8] of the corporation[9]: ______.<br>☒ Irrelevant (no provision set in the articles of association). | | |
| 3. | In the report year, an examination was held vis-à-vis the outside directors (and the independent directors) and it was found that in the report year they complied with the provision of Section 240(b) and (f) of the Companies Law regarding the absence of a link of the outside (and independent) directors holding office in the corporation, and that they also fulfill the conditions required for holding office as an outside (or independent) director. | ✓ | |
| 4. | All of the directors who held office in the corporation during the report year do not, directly or indirectly, report[10] to the CEO (excluding a director who is a workers' representative, if there is a workers' representative body in the corporation).If your answer is "Incorrect", (i.e., the director reports to the CEO as aforesaid) – state the number of directors not complying with the aforesaid restriction: ______. | ✓ | |
| 5. | All of the directors who notified of the existence of a personal interest they have in the approval of a transaction on the meeting's agenda, neither attended the deliberation nor participated in a vote as aforesaid (other than a deliberation and/or vote in circumstances as stated in Section 278(b) of the Companies Law):<br>If your answer is "Incorrect" –<br>Was it for the purpose of presentation of a specific issue by him pursuant to the provisions of the last part of Section 278(a): ☐ Yes ☐ No (check the appropriate box).<br>State the number of meetings in which such directors were present at the deliberation and/or participated in the vote, other than in circumstances as provided in Subsection a.: ___________. | ✓ | |

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[5] According to the language included in the document on proposed legislative amendments regarding improvement of the reports which was published by the Israel Securities Authority on March 16, 2014.
[6] In this questionnaire, "rate" – a specific number out of the total. For example 3/8.
[7] Including "outside directors" as defined in the Companies Law.
[8] In the context of this question – "articles of association" including pursuant to a specific legal provision that applies to the corporation (for example, in a banking corporation – the guidelines of the Supervisor of Banks).
[9] A bond company is not required to answer this section.
[10] For purposes of this question – the mere holding of office as a director in a held corporation which is controlled by the corporation, shall not be deemed as "reporting", conversely, a director's office in a corporation acting as an officer (other than a director) and/or employee in the held corporation which is controlled by the corporation, shall be deemed as "reporting" for purposes of this question.

| | | Correct | Incorrect |
|---|---|---|---|
| 6. | The controlling shareholder (including his relative and/or anyone on his behalf), who is not a director or another senior officer of the corporation, did not attend the board meetings held in the report year.<br>If your answer is "Incorrect" (i.e., the controlling shareholder and/or his relative and/or anyone on his behalf who is not a board member and/or a senior officer of the corporation attended such board meetings) - the following details regarding the attendance of any additional person in such board meetings shall be stated:<br>Identity: Ms. Stephanie Azrieli; Holds no position at the Corporation; the wife of Mr. David Azrieli OBM and the mother of Danna Azrieli, Chairman of the Board, Naomi and Sharon Azrieli, directors.<br>Was it for the purpose of presentation of a certain issue by him: □ Yes ☒ No (check the appropriate box)<br>The rate of his attendance[11] at board meetings held in the report year for the purpose of presentation of a specific issue by him: ___________.<br>Other presence: Ms. Stephanie Azrieli, accompanies her daughters, Danna Azrieli, Chairman of the Board, Naomi and Sharon Azrieli, directors; however, she does not take an active part in the discussions and resolutions. | | ✓ |

## Directors' qualifications and skills

| | | Correct | Incorrect |
|---|---|---|---|
| 7. | In the corporation's articles of association there is no provision limiting the possibility to immediately terminate the office of all of the directors of the corporation who are not outside directors (in this context - a determination by a regular majority is not deemed a limitation)[12].<br>If your answer is "Incorrect" (i.e., such limitation exists), state - | ✓ | |
| | a. The period prescribed in the articles of association for the office of a director: ______. | | |
| | b. The required majority prescribed in the articles of association for the termination of office of the directors: ______. | | |
| | c. The legal quorum at the general meeting prescribed in the articles of association for the termination of office of the directors: ______. | | |
| | d. The majority required for amending these provisions in the articles of association: ______. | | |
| 8. | The corporation has a training plan for new directors, in the field of the corporation's business and in the field of the law applicable to the corporation and the directors, as well as a continuing plan for the training of incumbent directors, which is adjusted, *inter alia*, to the position held by the director in the corporation.<br>If your answer is "Correct" - state whether the plan was implemented in the report year:☒Yes ☐ No (check the appropriate box) | ✓ | |
| 9. | a. The corporation determined a required minimum number of directors on the board who must have accounting and financial expertise.<br>If your answer is "Correct" – *state the minimum number which was determined: 1 (apart from the outside director having accounting expertise).* | ✓ | |
| | b. Number of directors holding office in the corporation during the report year -<br>Having accounting and financial expertise[13]: 4.<br>Having professional qualifications: 6.<br>*If there were changes in the number of directors as aforesaid in the report year, provide the figure of the lowest number (other than in the 60-day period from the change) of directors of any kind who held office in the report year.* | ✓ | |

11 While separating the controlling shareholder, his relative and/or another on his behalf.
12 A bond company is not required to answer this section.
13 After the board's estimation, in accordance with the provisions of the Companies Regulations (Conditions and Tests for Directors Having Accounting and Financial Expertise and Directors with Professional Qualifications), 5766-2005.

| | | | | |
|---|---|---|---|---|
| 10. | a. | Throughout the report year, the composition of the board included members of both genders.<br>If your answer is “Incorrect” – state the period (in days) in which the aforesaid was not met: ______.<br>In this question, you may answer “Correct” if the period in which directors of both genders did not hold office does not exceed 60 days. However, in any answer (Correct/Incorrect), state the period (in days) in which directors of both genders did not hold office in the corporation: 0. | ✓ | |
| | b. | Number of directors of each gender holding office on the board of the corporation as of the date of publication of this questionnaire:<br>Men: 5 Women: 4. | | |

## Board Meetings

| | | | Correct | Incorrect |
|---|---|---|---|---|
| 11. | a. | Number of board meetings held during each quarter in the report year:<br>Q1:4.<br>Q2:2.<br>Q3:2.<br>Q4:1. | | |
| | b. | Alongside each of the names of the directors holding office in the corporation during the report year, state their participation rate[14] in the board meetings (in this subsection - including meetings of the board committees of which they are members, and as stated below) held during the report year (in reference to his term of office):<br>*(Add extra lines according to number of directors)* | | |

| Name of Director | Rate of Participation in the Board Meetings (9 meetings) | Rate of Participation in the Meetings of the Audit Committee[17] (2 meetings) | Rate of Participation in the Meetings of the Financial Statements Review Committee[16] (4 meetings) | Rate of Participation in Meetings of Compensation Committee[15] (3 meetings) | Rate of Participation in Meetings of Additional Board Committees of which he is a Member (state the committee's name) |
|---|---|---|---|---|---|
| Danna Azrieli | 9/9 | | | | ---- |
| Naomi Azrieli | 9/9 | | | | ---- |
| Sharon Azrieli | 8/9 | | | | ---- |
| Joseph Ciechanover | 9/9 | 2/2 | 4/4 | 3/3 | Enforcement Committee – 1/1 |
| Oran Dror | 9/9 | 1/2 | 3/4 | 3/3 | Enforcement Committee – 1/1 |
| Niv Ahituv | 7/9 | 2/2 | 4/4 | 3/3 | Enforcement Committee – 1/1 |
| Efraim Halevy | 9/9 | 2/2 | 4/4 | 3/3 | Enforcement Committee – 1/1 |

14 See footnote 9.
15 With regard to a director who is a member of this committee.
16 With regard to a director who is a member of this committee.
17 With regard to a director who is a member of this committee.

| | | | | | |
|---|---|---|---|---|---|
| Tzipora Carmon | 9/9 | 2/2 | 4/4 | 3/3 | Enforcement Committee – 1/1 |
| Menachem Einan | 9/9 | 2/2 | 4/4 | 3/3 | Enforcement Committee – 1/1 |

| | | | |
|---|---|---|---|
| 12. | In the report year, the board held at least one deliberation on the management of the corporation's business by the CEO and the officers reporting to him, in their absence, and they were afforded the opportunity to express their position. | ✓ | |

## Separation between the Positions of the CEO and the Chairman of the Board

| | | Correct | Incorrect |
|---|---|---|---|
| 13. | Throughout the entire report year, a chairman of the board held office in the corporation.<br>In this question, you may answer "Correct" if the period in which a chairman of the board did not hold office in the corporation does not exceed 60 days, as provided in Section 363A(2) of the Companies Law). However, in any (Correct/Incorrect) answer, state –<br>The period (in days) during which there was no chairman of the board holding office in the corporation as aforesaid: ______. | ✓ | |
| 14. | Throughout the entire report year, a CEO held office in the corporation.<br>In this question, you may answer "Correct" if the period during which there was no acting CEO in the corporation does not exceed 90 days as provided in Section 363A.(6) of the Companies Law, however, in any (Correct/Incorrect) answer, state the period (in days) during which there was no CEO holding office in the corporation as aforesaid: ______. | ✓ | |
| 15. | In a corporation in which the chairman of the board also serves as the CEO of the corporation and/or exercises his powers, the dual office was approved in accordance with Section 121(c) of the Companies Law[18].<br>☒Irrelevant (insofar as such dual office does not exist in the corporation). | | |
| 16. | The CEO is not a relative of the chairman of the board. | ✓ | |
| 17. | A controlling shareholder or his relative do not serve as the CEO or as a senior officer in the corporation, other than as a director. | ✓ | |

[18] In a bond company – an approval pursuant to Section 121(d) of the Companies Law.

## The Audit Committee

| | | | Correct | Incorrect |
|---|---|---|---|---|
| 18. | The following did not hold office in the audit committee during the report year - | | | |
| | a. | The controlling shareholder or his relative. | ✓ | |
| | b. | The chairman of the board. | ✓ | |
| | c. | A director who is employed by the corporation or by the controlling shareholder of the corporation or by a corporation controlled by him. | ✓ | |
| | d. | A director who regularly provides services to the corporation or to the controlling shareholder of the corporation or a corporation controlled by him. | ✓ | |
| | e. | A director whose primary livelihood depends on the controlling shareholder. | ✓ | |
| 19. | No one who is not entitled to be a member of the audit committee, including a controlling shareholder or his relative, was present, in the report year, in the audit committee meetings, other than pursuant to the provisions of Section 115 (e) of the Companies Law. | | ✓ | |
| 20. | The Legal quorum for deliberation and adoption of resolutions in all of the audit committee's meetings held during the report year was a majority of the committee members, where the majority of the attendees were independent directors and at least one of them was an outside director.<br>If your answer is "Incorrect" - state the rate of the meetings in which the said requirement was not met: ______. | | ✓ | |
| 21. | In the report year, the audit committee held at least one meeting in the presence of the internal auditor and the outside auditor, and in the absence of officers of the corporation who are not members of the committee, regarding deficiencies in the business management of the corporation. | | ✓ | |
| 22. | In all of the audit committee's meetings in which a person who is not entitled to be a committee member was present, it was with the approval of the chairman of the committee and/or at the request of the committee (regarding the general counsel and secretary of the corporation who is not a controlling shareholder or his relative). | | ✓ | |
| 23. | In the report year, there were valid arrangements which were set forth by the audit committee regarding the manner of handling complaints of employees of the corporation in relation to flaws in the management of its business and with regard to the protection that will be provided to employees who complained as aforesaid. | | ✓ | |
| 24. | The audit committee and/or the Financial Statements Review Committee is satisfied that the scope of work of the auditor and his fee with respect to the financial statements in the report year were appropriate for the performance of proper audit and review work. | | ✓ | |

## The Duties of the Financial Statements Review Committee (hereinafter - FSRC) in its Preliminary Work for the Approval of the Financial Statements

| | | | Correct | Incorrect |
|---|---|---|---|---|
| 25. | a. | State the period (in days) prescribed by the board of directors as reasonable time for delivery of the committee's recommendations in contemplation of the board's deliberation for the approval of the financial statements: 2 business days apart from cases in which it is otherwise determined under the circumstances. | | |
| | b. | The number of days actually elapsed between the date of delivery of the recommendations to the board and the date of the board's deliberation for the approval of the financial statements:<br>Q1 statement (for 2018): 2.<br>Q2 statement: 2.<br>Q3 statement: 2.<br>Annual Statement: 2. | | |
| | c. | The number of days elapsed between the date of delivery of the draft financial statements to the directors and the date of the board's deliberation for the approval of the financial statements:<br>Q1 statement (2018): 6 days.<br>Q2 statement: 6 days.<br>Q3 statement: 6 days.<br>Annual statement: 6 days. | | |
| 26. | | The Corporation's outside auditor was invited to all of the FSRC and board meetings, in which the financial statements of the corporation referring to periods included in the report year were deliberated. | ✓ | |
| 27. | | All of the conditions specified below were fulfilled at the FSRC throughout the entire report year and until the release of the annual statement: | | |
| | a. | The number of the members was not less than three (on the date of the deliberation by the FSRC and approval of the statements as aforesaid). | ✓ | |
| | b. | All of the conditions specified in Section 115 (b) and (c) of the Companies Law (in respect of the office of audit committee members) were met thereby. | ✓ | |
| | c. | The chairman of the FSRC is an outside director. | ✓ | |
| | d. | All of its members are directors and most of its members are independent directors. | ✓ | |
| | e. | All of its members have the ability to read and understand financial statements and at least one of the independent directors has accounting and financial expertise. | ✓ | |
| | f. | The members of the FSRC provided a statement prior to their appointment. | ✓ | |
| | g. | The legal quorum for discussion and decision making on the FSRC was the majority of its members provided that most of those present were independent directors including at least one outside director. | ✓ | |

## Compensation Committee

| | | Correct | Incorrect |
|---|---|---|---|
| 28. | In the report year, the FSRC consisted of at least three members and the outside directors constituted a majority therein (on the date of the deliberation by the committee). | ✓ | |
| 29. | The terms of office and employment of all of the members of the compensation committee in the report year are in accordance with the Companies Regulations (Rules on Compensation and Expenses for an Outside Director), 5760-2000. | ✓ | |
| 30. | The following did not hold office in the compensation committee during the report year - | ✓ | |
| | a. The controlling shareholder or his relative. | ✓ | |
| | b. The chairman of the board. | ✓ | |
| | c. A director who is employed by the corporation or by the controlling shareholder of the corporation or by a corporation controlled by him | ✓ | |
| | d. A director who regularly provides services to the corporation or to the controlling shareholder of the corporation or a corporation controlled by him. | ✓ | |
| 31. | In the report year, a controlling shareholder or his relative did not attend meetings of the compensation committee, unless the chairman of the board determined that any one of them is required in order to present a specific issue. | ✓ | |
| 32. | The compensation committee and the board did not exercise their power pursuant to Sections 267A(c), 272(c)(3) and 272(C1)(1)(c) to approve a transaction or compensation policy, despite the objection of the general meeting. | ✓ | |

## Internal Auditor

| | | Correct | Incorrect |
|---|---|---|---|
| 33. | The chairman of the board or the CEO of the corporation is the organizational supervisor of the internal auditor in the corporation. | ✓ | |
| 34. | The chairman of the board or the audit committee approved the work plan in the report year.<br>In addition, specify the audit issues addressed by the internal auditor in the report year: In the year of the report, as in every year, the audit plan was preapproved by the audit committee and the board of directors of the Company, and as of the Report Release Date, the internal auditor has completed the reports according to plan, including on financial, operational and corporate governance issues. | ✓ | |
| 35. | Scope of employment of the internal auditor in the corporation in the report year (in hours[19]): According to the specification in Section 6 of Chapter E of the annual report above.<br>In the report year a deliberation was held (by the audit committee or the board) on the internal auditor’s findings. | ✓ | |
| 36. | The internal auditor is neither an interested party in the corporation, nor its relative, auditor or another on its behalf, nor maintains material business ties with the corporation, its controlling shareholder, relative or corporations controlled thereby. | ✓ | |

[19] Including working hours invested in held companies and in auditing overseas, and as the case may be.

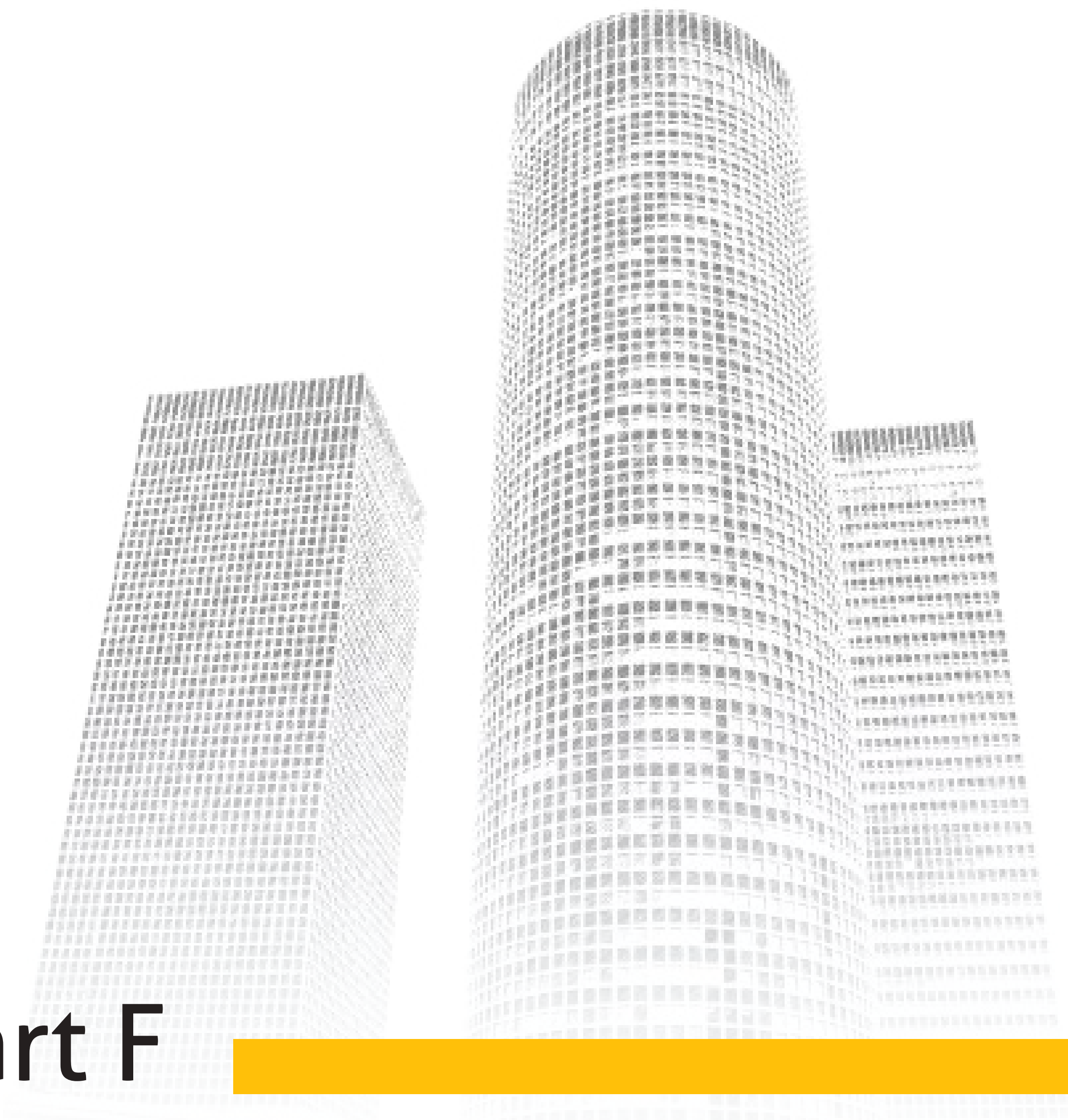
## Transactions with Interested Parties

| | | Correct | Incorrect |
|---|---|---|---|
| 37. | The controlling shareholder or his relative (including a company controlled by him) is neither employed by the corporation nor provides management services thereto.<br>If you answer is "Incorrect" (i.e. the controlling shareholder or his relative is employed by the corporation or provides management services thereto) state -<br>– The number of relatives (including the controlling shareholder) employed by the corporation (including companies controlled by them and/or through management companies): 1 (Ms. Danna Azrieli).<br>– Have the agreements for such employment and/or management services been approved by the organs specified in the law:<br>☒ Yes (the management agreement with Ms. Danna Azrieli, who serves as the Company's Active Chairman of the Board, was approved by the compensation committee, the board of directors and the general meeting of the Company held in October 2016).<br>☐ No | | ✓ |
| 38. | To the best knowledge of the corporation, the controlling shareholder does not have other businesses in the operating segment of the corporation (in one or more segments).<br>If your answer is "Incorrect" - state whether an arrangement was prescribed to define activities between the corporation and the controlling shareholder thereof:<br>☒Yes, see specification on the arrangement to define activity in Section 3.2 above.<br>☐ No | | ✓ |

Chairman of the Board: Ms. Danna Azrieli    Chairman of the Audit Committee: Efraim Halevy    Chairman of the FSRC: Prof. Niv Ahituv

AZRIELIGROUP

# Effectiveness of Internal Control over the Financial Reporting and Disclosure



# Part F

# ATTACHED HERETO IS AN ANNUAL REPORT ON THE EFFECTIVENESS OF INTERNAL CONTROL OVER FINANCIAL REPORTING AND DISCLOSURE PURSUANT TO REGULATION 9B(A) FOR 2018:

The management, under the supervision of the Board of Directors of Azrieli Group Ltd. (the "Corporation"), is responsible for setting and maintaining proper internal control over financial reporting and disclosure at the Corporation.

For this purpose, the members of management are:

1 | Eyal Henkin, CEO

2 | Irit Sekler-Pilosof, CFO

3 | Ran Tal, VP, General Counsel and Corporate Secretary

4 | Yair Horesh, Chief Comptroller for Accounting and Financial Statements

Internal control over financial reporting and disclosure consists of controls and procedures existing at the Corporation, designed by, or under the supervision of, the CEO and the most senior financial officer, or by anyone actually performing such functions, under supervision of the Board of Directors of the Corporation, which are designed to provide reasonable assurance regarding the reliability of the financial reporting and the preparation of the reports according to the provisions of the law, and to ensure that information which the Corporation is required to disclose in reports released thereby according to the law is gathered, processed, summarized and reported within the time frames and in the format set forth by the law.

Internal control includes, *inter alia*, controls and procedures designed to ensure that information which the Corporation is thus required to disclose, is gathered and transferred to the management of the Corporation, including the CEO and the most senior financial officer, or anyone actually performing such functions, in order to enable the timely decision making in reference to the disclosure requirement

Due to its inherent limitations, internal control over financial reporting and disclosure is not designed to provide absolute assurance that misrepresentation or omission of information in the reports is avoided or discovered.

The management, under the supervision of the Board of Directors, carried out an examination and evaluation of internal control over financial reporting and disclosure at the Corporation, and the effectiveness thereof. The evaluation of the effectiveness of internal control over financial reporting and disclosure carried out by the management under the supervision of the Board of Directors included:

- Mapping and documentation of the controls and identification of the very material processes at the Company and at the main consolidated companies according to the reporting risks, in respect of each of the Company or the main consolidated companies, as the case may be.
- The processes which were defined as very material are: in the Company: revenues from rent in investment property, investment property; in Supergas: the revenues from sales process.
- Examination of the actual performance and documentation of the controls defined in the control processes on the organization level (ELC), the information systems (ITGC), the financial statements preparation process and the processes which were identified as very material to the financial reporting and disclosure.
- General evaluation of the internal control effectiveness.
- Based on the effectiveness evaluation performed by the management with the supervision of the Board of

Directors as specified above, the Board of Directors and management of the Corporation reached the conclusion that internal control over financial reporting and disclosure in the Corporation, as of December 31, 2018 is effective.

Attached please find the statements of the CEO and the CFO, who is responsible for the financial reporting in the Company.

Date: March 19, 2019

## STATEMENT OF MANAGERS:

### STATEMENT OF CEO PURSUANT TO REGULATION 9B(D)(1):

I, Eyal Henkin, represent that:

1. I have reviewed the periodic report of Azrieli Group Ltd. (the "Corporation") for the year 2018 (the "Reports").
2. To my knowledge, the Reports do not contain any misrepresentation nor omission of a material fact required for the representations included therein, given the circumstances under which such representations were included, not to be misleading with regard to the period of the Reports.
3. To my knowledge, the Financial Statements and other financial information included in the Reports adequately reflect, in all material respects, the financial position, operating results and cash flows of the Corporation for the periods and as of the dates covered by the Reports.
4. I have disclosed to the Corporation's auditor and to the Corporation's Board of Directors and the Audit Committee and Financial Statement Committee, based on my most current evaluation of internal control over financial reporting and disclosure:
   a. Any and all significant flaws and material weaknesses in the setting or maintaining internal control over financial reporting and disclosure which may reasonably adversely affect the Corporation's ability to gather, process, summarize or report financial information in a manner which casts doubt on the reliability of the financial reporting and preparation of the Financial Statements in conformity with the provisions of the law; and –
   b. Any fraud, either material or immaterial, which involves the CEO or anyone reporting to him directly or which involves other employees who play a significant role in internal control over financial reporting and disclosure;
5. I, myself or jointly with others at the Corporation:
   a. Have set controls and procedures, or confirmed, under my supervision, the setting and maintaining of controls and procedures which are designed to ensure that material information in reference to the Corporation, including consolidated companies thereof as defined in the Securities Regulations (Annual Financial Statements), 5770-2010, is brought to my knowledge by others at the Corporation and the consolidated companies, particularly during the preparation of the Reports; and –
   b. Have set controls and procedures, or confirmed, under my supervision, the setting and maintaining of controls and procedures which are designed to reasonably ensure reliability of financial reporting and preparation of the Financial Statements in conformity with the provisions of the law, including in conformity with GAAP.
   c. Have evaluated the effectiveness of internal control over financial reporting and disclosure and presented in this report the conclusions of the Board of Directors and management with regard to the effectiveness of internal control as aforesaid as of the date of the Reports.

The aforesaid does not derogate from my responsibility or from the responsibility of any other person, pursuant to any law.

Date: March 19, 2019

Eyal Henkin | CEO

## STATEMENT OF MANAGERS:

### STATEMENT OF THE MOST SENIOR FINANCIAL OFFICER PURSUANT TO REGULATION 9B(D)(2):

I, Irit Sekler-Pilosof, represent that:

1. I have reviewed the Financial Statements and other financial information included in the reports of Azrieli Group Ltd. (the "Corporation") for year 2018 (the "Reports");
2. To my knowledge, the Financial Statements and the other financial information included in the Reports do not contain any misrepresentation nor omission of a material fact required for the representations included therein, given the circumstances under which such representations were included, not to be misleading with regard to the period of the Reports.
3. To my knowledge, the Financial Statements and other financial information included in the Reports adequately reflect, in all material respects, the financial position, operating results and cash flows of the Corporation for the periods and as of the dates covered by the Reports;
4. I have disclosed to the Corporation's auditor and to the Corporation's Board of Directors and the Audit Committee and Financial Statement Committee, based on my most current evaluation of internal control over financial reporting and disclosure:
    a. Any and all significant flaws and material weaknesses in the setting or maintaining internal control over financial reporting and disclosure insofar as it relates to the Financial Statements and the other information included in the Reports, which may reasonably adversely affect the Corporation's ability to gather, process, summarize or report financial information in a manner which casts doubt on the reliability of financial reporting and preparation of the Financial Statements in conformity with the provisions of the law; and -
    b. Any fraud, either material or immaterial, which involves the CEO or anyone reporting to him directly or which involves other employees who play a significant role in internal control over financial reporting and disclosure;
5. I, myself or jointly with others at the Corporation:
    a. Have set controls and procedures, or confirmed, under my supervision, the setting and maintaining of controls and procedures, which are designed to ensure that material information in reference to the Corporation, including consolidated companies thereof as defined in the Securities Regulations (Annual Financial Statements), 5770-2010, insofar that it is relevant to the financial statements and other financial information included in the Reports, is brought to my knowledge by others at the Corporation and the consolidated companies, particularly during the preparation of the Reports; and -
    b. Have set controls and procedures, or confirmed, under my supervision, the setting and maintaining of controls and procedures which are designed to reasonably ensure reliability of financial reporting and preparation of the Financial Statements in conformity with the provisions of the law, including in conformity with GAAP;
    c. Have evaluated the effectiveness of internal control over financial reporting and disclosure, insofar as it relates to the Financial Statements and the other financial information included in the Reports, as of the date of the Reports. My conclusions in respect of my evaluation as aforesaid were presented to the Board of Directors and management and are incorporated in this Report.

The aforesaid does not derogate from my responsibility or from the responsibility of any other person, pursuant to any law.

Date: March 19, 2018

Irit Sekler-Pilosof | CFO