

# MEMO

To: Ester Levanon, CEO Tel Aviv Stock Exchange

From: Elizabeth Hershman, Chief Financial Officer NASDAQ OMX Group, Inc.

CC: Richard Linowes, Professor American University Kogod School of Business

Date: November 21, 2014

Re: The NASDAQ OMX Group, Inc. Proposed Acquisition of the Tel Aviv Stock Exchange.

## EXECUTIVE SUMMARY

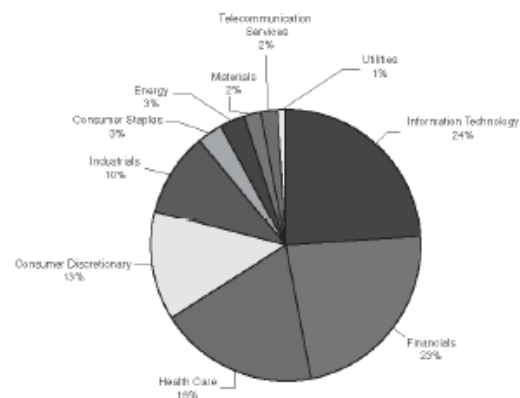
The NASDAQ stock exchange prides itself in its proprietary technology that allows companies access to capital so that they can compete globally. As a means to expand, the NASDAQ recently acquired the OMX Nordic exchange to form what is now known as the NASDAQ OMX Group, Inc. This allowed the NASDAQ to gain exposure to markets in Europe and provided a way for the NASDAQ to enter the international arena. With the high tech capabilities of the Tel Aviv Stock Exchange, many Israeli companies are looking to it to provide them with a way to raise capital in the public markets. After raising sufficient capital to meet the regulations set forth by markets such as the NASDAQ, many companies that list on the Tel Aviv Exchange choose to co-list themselves on the NASDAQ through ADRs. With the number of companies co-listing on both the NASDAQ and the TASE, the relationship between the two exchanges has continued to grow. The signing of the Memorandum of Understanding in November 2007 was a public demonstration of the partnership between the two organizations. Therefore, it is only natural that the next step in this partnership is the NASDAQ buyout of the Tel Aviv Exchange which will mutually benefit both parties involved.

## ABOUT THE NASDAQ OMX GROUP, Inc.

The NASDAQ OMX Group, Inc. (NASDAQ) is the world's largest exchange company. It offers capital raising solutions to companies on both domestic and global scales. This includes the United States listing market, the OMX Nordic Exchanges, and the 144A PORTAL Market. The NASDAQ offers trading amongst various types of securities which include equities, derivatives, debt, commodities and exchange traded funds (ETFs). Its technology platform supports the operations of exchanges and clearing houses in over fifty countries across the world.

As the largest U.S. electronic stock market, the NASDAQ has over 3,100 listed companies which

Percentage of Nasdaq-listed Companies by Industry



account for 21.4 billion shares traded.<sup>1</sup> The average trading volume on the NASDAQ over the past the years has been around 2.7 million shares with highs of four million shares in the early 2000s during the “dot.com” era. While the trading volume in shares has remained relatively stable, the percentage of the overall trading done on the NASDAQ has continued to climb. This shows that the market is starting to look at the electronic communications networks as a more favorable means for trading. The ownership of the NASDAQ is made up of primarily institutions and insiders. Institutions constitute over 95% of the ownership and insiders own over 40%. Due to this ownership, the NASDAQ does not pay out dividends to shareholders; rather, it uses its retained earnings to continue to improve its business through investing in high technology, cutting edge equipment that will enhance the value of the services it is able to provide to its clients.<sup>2</sup>

## CURRENT RELATIONSHIP BETWEEN THE NASDAQ AND TASE

During 2006, the Tel Aviv Exchange was helped by Israel's high economic growth and stable prices. Export industries continued to be the leaders in economic growth and with the lowering of interest rates by the Bank of Israel, the outlook for 2007 was very positive. With positive economic conditions, the TASE was able to thrive with increased turnover in trading volume for both stocks and options. In addition to its domestic success, the TASE was able to continue to promote its strategic objectives such as expanding its clearing house, introducing new products and continuing its relationship with the NASDAQ.<sup>3</sup>

The Tel Aviv Stock Exchange and NASDAQ have a strong relationship which was formalized in November 2007 with the signing of an agreement to form a closer working relationship for companies listed on both exchanges. The Memorandum of Understanding (MOU) stated that the NASDAQ and TASE will work to facilitate stronger trading and allow better access to more capital for the firms listed. The MOU formalized the ongoing relationship that the TASE has had with the NASDAQ. Currently, after 27 years of strong commitments to the TASE the NASDAQ has 70 Israeli companies listed on the exchange. These companies have a combined global market cap of over \$60 billion.



Companies that currently list on both exchanges include big names like Teva Pharmaceuticals. If a company chooses to list first on the TASE then on the NASDAQ its shares are listed as ADRs; however, if a company chooses to go public in the US and then list on the TASE, its shares are listed as any American company's shares would be. Recently, due to Israel's brisk economic growth of 5.3% in 2007, Barclay's has announced the iShares MSCI Israel Index Fund (IES).<sup>4</sup>

## NASDAQ PROPOSAL TO ACQUIRE THE TASE

Based on the current positions of the NASDAQ and the Tel Aviv Stock Exchange, the NASDAQ's proposed acquisition of the TASE will benefit each party involved. The two exchanges already are collaborating as was demonstrated in the signing of the MOU in 2007. Because each exchange prides itself in its cutting edge technological capabilities and due to both exchanges' potential for growth, this acquisition seems to be a natural next step to ensuring the long term success of each exchange. The NASDAQ will acquire the TASE as a wholly owned subsidiary of the current NASDAQ OMX Group, Inc.

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<sup>1</sup> [http://www.nasdaq.com/newsroom/stats/Performance\\_Report.stm](http://www.nasdaq.com/newsroom/stats/Performance_Report.stm)

<sup>2</sup> <http://finance.yahoo.com/q/ks?s=NDAQ>

<sup>3</sup> TASE 2006 Annual Report

<sup>4</sup> <http://seekingalpha.com/article/70821-new-ishares-israel-fund-heavy-on-teva-but-worth-a-look?source=yahoo>

The TASE's vision is to "promote business ethics in the capital markets in general and in its listed companies in particular, and to boost public confidence in the field of investments." It does this through providing sophisticated technological trading platforms and products to its clients. This meshes well with the NASDAQ's vision of "delivering multi-asset, multi service capability across six continents." NASDAQ OMX does this by using innovative services and technology. Since both of the exchanges' focus on technology and have similar visions, through combining the two, the synergy will create an even better, more beneficial organization for both parties involved.

## ENVIRONMENTAL SCAN

The current political situation in Israel as of 2008 has not prevented the TASE and Israeli economy from being successful. According to Israeli business executives, the security situation in Israel only influences investment decisions when war breaks out in a region. Nonetheless, one measurable impact of the security situation is that sometimes foreign corporate representatives refuse to travel to Israel to meet with local firms. As a consequence, this sometimes has resulted in a hampered partnership agreement.<sup>5</sup> While peace talks are continually on the agenda for both the Israelis and their neighbors, the political environment in Israel has been relatively the same since its declaration as a state in 1948 and therefore should not have an impact on the decision of the NASDAQ to invest in Israel.

In the United States, as of 2008 the political situation is slightly uncertain due to the upcoming presidential election. However the infrastructure of the country has been stable due to the rules and laws set forth in America. While the change in politicians may have some an effect on the economy in the short term, the political situation should not have a large impact on the markets in the United States. This should not have a significant impact on the deal between the NASDAQ and the TASE.<sup>6</sup>

Israel's economy continues to be successful despite the downturn of many major world economies. Over 2007, Israel's economy has grown by 5.1%, the shekel has appreciated against the dollar and other leading currencies, share prices of the TASE have soared about 40% and foreign investors have invested record amounts into Israeli real estate, equities and bonds. Due to the market conditions in the United States since the sub-prime crisis in summer 2007, with markets at record lows, the dollar's continual depreciation and liquidity issues, the strength of the Israeli economy would provide the NASDAQ with a way to hedge its exposure to the US economic decline and would offer a way for the growing company to further diversify itself and enter into a new world market. The NASDAQ has continued to be successful due to its expansion outside the US with mergers such as the OMX one. The TASE would just work to enhance the value of the NASDAQ exchange.

Both the US and Israel have free market economies and have similar laws regulating the trading of securities. Therefore, entrance into this market will not cause the NASDAQ to have to change its rules and regulations to meet those of the TASE and vice versa with the TASE and the NASDAQ. Looking at the environment in both Israel and the US shows that the NASDAQ-TASE merger should prove profitable and beneficial for both parties involved.

## TYPE OF ACQUISITION

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<sup>5</sup> <http://mba.tuck.dartmouth.edu/pecenter/research/pdfs/israel.pdf>

<sup>6</sup> <http://mba.tuck.dartmouth.edu/pecenter/research/pdfs/israel.pdf>

Currently the TASE is a privately owned company limited by guarantee. Its owners are its members which include both banks and non-bank institutions. The exchange is regulated by the Israel Securities Authority (ISA).<sup>7</sup> In order to acquire the TASE, the NASDAQ will be the owner of the TASE which will function as a wholly owned subsidiary. The value of the TASE according to its balance sheet as of December 1, 2006 was 718.3 million NIS. Accounting for the 5.3% growth rate in 2007 the value of the exchange as of January 1, 2008 was 756.4 million NIS (which is \$209.5 million). Because of the value add to the NASDAQ due to the goodwill and intangible assets currently available from this acquisition, the NASDAQ costs will be 210 million dollars up front plus an agreement which offers the TASE board members seats on the NASDAQ exchange and a percentage of the revenues made through the trading of TASE members on the Israeli exchange. Currently 60 of the approximate 700 companies listed on the TASE are co-listed on the NASDAQ. With the new abilities companies will have to trade on both exchanges, this number is expected to grow dramatically.

## DIFFERENCES BETWEEN THE TASE AND NASDAQ

One challenge that may arise is the difference between the two trading platforms. However, because over sixty of the firms that are listed on the Tel Aviv Exchange are co-listed on the NASDAQ, the two trading systems are already working together. The technologies used by each system are compatible and therefore, a transition to one unified system should be relatively easy. The current IT employees should be able to understand the others' systems and will be utilized to make the one common system even better. Instead of competing with one another, the two teams will be able to collaborate and share their skills and abilities.

Another challenge that may arise has to do with the cultural differences of the people in Israel compared to the people in the US and the corporate cultures between the two exchanges. However, due to their current relationship, this issue does not seem to be one that should cause major problems. To avoid any kind of minor problems that may come about when combining the two companies, the NASDAQ should hire organizational change experts or consultants that can assist in the merger strategy. It is important that each organization agrees upon the way the new business will be run. By hiring a business consultant, he or she can work with the management of both the TASE and the NASDAQ to collaborate and decide on a common set of corporate values and ideals. This process will take about three to six months and will take place prior to the official merger of the two companies. The average price for a consultant is \$100-\$150 per hour so in total this will cost the company less than \$1M.

Because the TASE is currently a closely held company where its members are the only shareholders and the NASDAQ is public, the transition from a "private" corporation to a public one could cause some of the TASE board members to lose some of their ownership. With the collaboration between the TASE board and the NASDAQ board, the members of the exchange will be able to understand the consequences of going public before they see the results. While this may cause the original board members of the TASE to sacrifice some profits, in the long term both parties will hopefully be more profitable due to their combined efforts. It is just important that each party understands how the organization will be run and each party's distinct responsibilities.

Other risks associated with this type of acquisition are the threat of the smaller company essentially being swallowed by the larger company and instead of profiting going under. The market cap of the TASE-100 which is the largest 100 companies listed on the TASE is 564.5 million and has an index value of 989.4 million NIS (\$260.2 million) while the market cap of the NASDAQ-100 is \$1798.72 million. This shows the relative size of the two organizations. The NASDAQ-100 is approximately seven times the size of the TASE. Therefore, the risk of

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<sup>7</sup> <http://www.tase.co.il/TASEEng/AboutTASE/Overview/>

losing profits short term is a realistic possibility. Yet, in the long term, this acquisition should prove profitable for both parties involved.

From the NASDAQ point of view, they face the risk that, being the larger company, the TASE could, if it is hurt, bring the NASDAQ down with it. This has happened in many mergers in the past. One example is the AOL/Time Warner merger. While Time Warner predicted that the AOL acquisition would be profitable, the results of the merger showed otherwise. There is no evidence at this time that seems to indicate the TASE could hurt the NASDAQ; rather, the evidence suggests that both exchanges could help each other. Although this scenario does not seem likely, it is still a risk that the NASDAQ could face and therefore should be considered before the merger. At this time it seems as though both the Tel Aviv Exchange and the NASDAQ will benefit from being one combined exchange.

#### Benefits to TASE

Through this transaction, both parties will benefit. The major benefits to the TASE include the strength of the NASDAQ in comparison with the TASE. Although the TASE currently offers local firms IPO and private placement options, relative to the NASDAQ and other major markets, the TASE suffers from low valuation multiples and low post-IPO liquidity.<sup>8</sup> Local Israeli firms that are planning IPOs traditionally target the more developed markets in the US or Europe. The CEO of the TASE, Ester Levanon's goal is to take the TASE global and promote the country in a way so that "an Israeli company would not need to go to foreign markets just to get a good valuation".<sup>9</sup> Through the NASDAQ acquisition, the TASE will be a more attractive market for Israeli investors looking to raise capital. It will have the strength and the liquidity of the NASDAQ backing the TASE which will enable it to grow more in the future.

Over sixty companies are currently co-listed on the Tel Aviv Exchange and the NASDAQ. In order for a company to list itself on more than one exchange, not only does the company have to meet each exchange's requirements but also, the company must pay fees to each exchange. This means that many of the Israeli firms are paying twice to list their company both locally and internationally (ie. on the NASDAQ). For many Israeli firms, it is easier for them to meet the requirements set forth by the SEC for foreign companies under the guidelines of the 20-F than it is for them to meet the requirements of the TASE. Therefore, many companies are choosing to list themselves on the NASDAQ and not on their home exchange. Through the proposed acquisition of the TASE, the fees associated with co-listing securities will be eliminated. This will enable the companies to raise their initial capital in the local market and to help the overall Israeli economy. Yet it will not hurt their exposure to global investment due to their ability to freely list themselves simultaneously on the NASDAQ. With the name and recognition of the NASDAQ backing the company, there will be more investor confidence and more investment will flow into Israel from abroad.

In addition to benefiting companies wishing to list their stock both domestically and internationally, the freedom to move between the NASDAQ and the TASE would benefit investors. Currently investors who invest outside of the Israeli markets are taxed on earnings as capital gains at a rate of 35% while if they invest in companies listed on the TASE they avoid all capital gains tax. By allowing investors to invest on the NASDAQ free of capital gains tax, or with more competitive capital gains tax rates, this will increase the amount of investment opportunities for individuals while simultaneously increasing the volume on both exchanges.

As the two exchanges stand now, there are separate listing requirements for both exchanges. With the proposed merger, the requirements will be the same and will follow those of the NASDAQ exchange due to its size and strength in the global market. This will

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<sup>8</sup> <http://mba.tuck.dartmouth.edu/pecenter/research/pdfs/israel.pdf>

<sup>9</sup> <http://www.worldbusinesslive.com/Finance/Article/739782/tel-aviv-stock-exchange-comes-age/>

ensure that companies can take advantage of the opportunities available through listing on the NASDAQ and will allow the NASDAQ to take advantage of their exposure to the markets in the Middle East.

Most of the companies listed on the TASE currently are local Israeli companies. While some of them are large in size (such as Teva Pharmaceuticals which is \$36.18 billion) the majority of them are less than \$10 billion. As firms want to expand, many of them are either bought out or acquired by larger US and international firms which are listed on the NASDAQ because the TASE cannot handle the large scale M&A activity. Through using the existing capabilities of the NASDAQ, the TASE will be able to become a more viable option for Israeli firm expansion and M&A activities. This will help the TASE to grow and to attract more foreign investment. Through the TASE/NASDAQ merger, the economic situation in Israel, which itself has improved tremendously since 2002, will continue to improve and develop into a globally competitive economy.

## HOW TO COMPENSATE TASE OWNERS

As the Tel Aviv Stock Exchange is currently a member owned exchange, the owners will now have to be properly compensated by the NASDAQ. Because the NASDAQ is public, the most efficient and fair way to compensate the once members of the exchange is to make these members now shareholders. As was the way the New York Stock Exchange went public, the members became shareholders thus aligning their interests with the overall interest of the firm.<sup>10</sup> Because the traders will now be owners of the NASDAQ stock exchange, they will profit based on profitable strategic advances that the NASDAQ does. While the board members will now become stock holders, and the current CEO of the TASE will now become a board member on the NASDAQ, the current management and board of the TASE will remain in tact and will ensure that the TASE continues to run successfully. This will ease the transition as many of the board members of the TASE are very familiar with the way the NASDAQ works given the two exchanges' close relationship and given that many of the companies listed on the TASE are already co listed on the NASDAQ.

## COSTS ASSOCIATED WITH THE ACQUISITION

The costs associated with the Tel Aviv Stock Exchange acquisition are \$250 million dollars. This cost has been calculated by using the book value of the TASE assets and taking a percentage of the trades based on the market cap of the TASE in comparison of that of the NASDAQ. In addition to the upfront acquisition costs, 60% of the revenue from each trade that is made by a company that is listed solely on the TASE will be divided amongst the former TASE board members. For shares that are co-listed on the exchange, the profits will be equally distributed. For firms that decide to go public on the TASE exchange as opposed to the NASDAQ, the former TASE board members will receive 50% of the profits from this transaction. This will benefit both parties involved because, while the TASE is giving up its autonomy, they are going to be benefiting from being a part of the NASDAQ. The NASDAQ will benefit because the revenues they receive will be more than what they would have received had they not acquired the Tel Aviv Exchange and also because of their ability to enter a new global market.

## RISKS

The major risk of the NASDAQ-TASE merger is its regulatory approval. Although the laws concerning the securities markets are similar in the US and Israel, the governments in each

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<sup>10</sup> <http://knowledge.wharton.upenn.edu/article.cfm?articleid=1428>

respective country must approve of this deal. With the recent expansion of the NASDAQ through the OMX deal, the NASDAQ has taken the position of being the largest player in securities trading in the world. Any further expansion could potentially cause a violation of the anti-trust laws in the US or other global laws which work to ensure a fair market for competition. In Israel, the government has a stake in the TASE due to the large number of business people being involved in the political spectrum.

Another risk is that the benefits foreseen in this merger—namely the free movement between the exchanges and the growth potential of each party involved—may not be as great as is predicted. While there seems to be a large growth potential for each institution, the merger could see not as rapid an expansion as anticipated due to lack of demand for the new trading platform or simply due to the fact that the market situation is not favorable. The economic trends that have hit the United States since the sub-prime crisis in 2007 could have a greater impact in Israel with this proposed merger. With the US domestic market being not as strong, and the Israeli market being now closely linked to the US market, the Israeli market has the potential to suffer when the U.S. market is suffering. This could have a larger impact on the Israeli economy due to its size relative to that of the US economy. Also, if the Israeli economy were to be hurt then this may be felt in the United States as well.

Further risks have to do with any international merger and include currency risk, economic risk and political risk. Currently the TASE is valued in shekels and the NASDAQ is valued in dollars. Therefore, when conducting international business, the currency risk has to be taken into consideration. One solution to this problem is for the Israeli exchange to switch its denomination to dollars; however, that transition will take time and will require that Israel switch its currency to the dollar. At this time that does not seem like a viable solution since the dollar is in a period of decline and the Shekel, and the Israeli economy as a whole is in a period of growth. The currency risk is nothing new; international companies have to deal with using different currencies all the time and through using forward or futures contracts, there are ways to hedge currency exposure. Therefore, this risk is not a major one and should not have a large impact on the proposed merger.

Other risks include the risks associated with dealing with people in different countries. These include the risks that the NASDAQ or TASE will not see eye to eye on each of their goals and objectives, the different roles of the two organizations may not be understood by each party, and that the parties fail to exercise due diligence. Since the NASDAQ is the bigger of the two organizations, and it will be the controlling body of the new entity, it has more to lose than the TASE if anything goes wrong. Oftentimes there are differences that may arise in the organization of the two parties. In this merger, although the NASDAQ will be the overseeing body, the TASE will be able to maintain its same organizational structure. The only difference will be that the NASDAQ will have seats on the TASE board and the TASE will now be an active part of the NASDAQ leadership team.

The economic and political risks associated with this merger are the uncontrollable movements in both the Israeli and US markets and the political situation particularly in Israel. While the markets in Israel have managed to remain relatively unaffected by the political situation, there is still a risk that they may be affected in the future due to war or other political events that are unpredictable at the current time. These risks however, are ones that should be taken into consideration and be looked at as potential risks for the future but at this time they do not seem as though they should have an impact on the merger.

## FUTURE MANAGEMENT

The future management of the acquired Tel Aviv Exchange will not differ from the current management of the TASE. While the TASE will be a wholly owned subsidiary of the NASDAQ, it will keep its same management and organizational structure. There will be

communication amongst the top management of the TASE and the NASDAQ to ensure that the two exchanges are running harmoniously. Also, the IT departments will become one department and the trading platforms will be developed together to ensure that companies can easily transport from one exchange to another if they so choose.

## FUTURE DIRECTION OF COMBINED EXCHANGE

TASE as wholly owned subsidiary of NASDAQ OMX would be a beneficiary of the economies of scale of the larger organization and have access to funds and resources of the larger organization. This includes access to the NASDAQ's resources and relationships with banks and other financial intermediaries. If the TASE needs credit to expand to other countries, it can now tap into the NASDAQ international lines of credit. The brand image of the NASDAQ will also be beneficial as the TASE exchange grows. The TASE will go from being a completely domestic exchange to a global exchange due to its new relationship with the NASDAQ.

The NASDAQ will benefit from this new acquisition as well. The NASDAQ will now have exposure to new markets in an area that is hard to enter alone. It will be able to hedge its exposure to these markets through the TASE exchange. Companies that want to list on the NASDAQ can first list on the TASE exchange to prove their financial strengths. Then, the companies can easily transition to the NASDAQ. With the direction of the US economy in comparison with the world economy, the exposure to different markets in different parts of the world can help the NASDAQ to hedge its risks associated with currency fluctuations and market movements.



## EXHIBITS

### Selected Consolidated Financial Data

	Year Ended December 31,				
	2006	2005	2004	2003	2002
	(in thousands, except share and per share amounts)				
<b>Statements of Income Data:</b>					
Total revenues <sup>(1)</sup>	\$ 1,657,776	\$ 879,919	\$ 540,441	\$ 589,845	\$ 787,154
Cost of revenues <sup>(1)</sup>	(970,381)	(353,908)	(55,845)	—	—
Gross margin	687,395	526,011	484,596	589,845	787,154
Total expenses	473,306	412,348	476,413	647,159	675,307
Net income (loss) from continuing operations	127,893	61,690	1,804	(45,112)	65,021
Net income (loss) from discontinued operations, net of taxes <sup>(2)</sup>	—	—	9,558	(60,335)	(21,893)
Net income (loss)	127,893	61,690	11,362	(105,447)	43,128
Net income (loss) applicable to common stockholders	127,203	55,093	(1,826)	(113,726)	33,363
Basic and diluted earnings (loss) per share:					
Basic earnings (loss) per share:					
Continuing operations	\$ 1.22	\$ 0.68	\$ (0.14)	\$ (0.68)	\$ 0.66
Discontinued operations	—	—	0.12	(0.77)	(0.26)
Total basic earnings (loss) per share	\$ 1.22	\$ 0.68	\$ (0.02)	\$ (1.45)	\$ 0.40
Diluted earnings (loss) per share:					
Continuing operations	\$ 0.95	\$ 0.57	\$ (0.14)	\$ (0.68)	\$ 0.66
Discontinued operations	—	—	0.12	(0.77)	(0.26)
Total diluted earnings (loss) per share	\$ 0.95	\$ 0.57	\$ (0.02)	\$ (1.45)	\$ 0.40
Weighted average common shares outstanding for earnings (loss) per share:					
Basic	104,311,040	80,543,397	78,607,126	78,378,376	83,650,478
Diluted	144,228,855	111,913,715	78,607,126	78,378,376	84,073,381
	December 31,				
	2006	2005	2004	2003	2002
	(in thousands)				
<b>Balance Sheets Data:</b>					
Cash and cash equivalents and available-for-sale investments <sup>(3)</sup>	\$ 1,950,204	\$ 344,606	\$ 233,099	\$ 334,633	\$ 423,588
Total assets <sup>(4)</sup>	3,716,452	2,046,786	814,820	851,254	1,175,914
Total long-term liabilities <sup>(5)</sup>	1,798,466	1,467,453	449,941	452,927	636,210
Total stockholders' equity <sup>(6)</sup>	1,457,355	253,007	156,563	160,696	270,872

**THE TEL-AVIV STOCK EXCHANGE LTD**

**BALANCE SHEETS**

**(NIS in thousands)**

	Note	Consolidated		Company	
		December 31,		December 31,	
		2006	(*)2005	2006	2005
<b>Current assets</b>					
Cash and cash equivalents	3	26,145	17,264	16,548	12,372
Marketable securities	4	171,535	152,304	87,206	98,821
Trade accounts receivable	5	1,420	1,087	1,420	1,087
Receivables with respect to open derivative positions	6	329,499	-	-	-
Assets with respect to securities that were not transferred to the Stock Exchange Clearing House on a timely basis	7	143,001	-	-	-
Receivables and other current assets	8	11,299	8,572	10,215	10,816
		<u>682,899</u>	<u>179,227</u>	<u>115,389</u>	<u>123,096</u>
<b>Investments</b>					
Subsidiaries	9	-	-	91,779	51,892
Affiliate	10	4,089	4,137	4,089	4,137
		<u>4,089</u>	<u>4,137</u>	<u>95,868</u>	<u>56,029</u>
<b>Other assets</b>	9	<u>492</u>	<u>-</u>	<u>-</u>	<u>-</u>
<b>Fixed assets</b>	11				
Cost		139,862	125,124	139,862	125,124
Less: accumulated depreciation		<u>109,066</u>	<u>101,740</u>	<u>109,066</u>	<u>101,740</u>
		<u>30,796</u>	<u>23,384</u>	<u>30,796</u>	<u>23,384</u>
		<u>718,276</u>	<u>206,748</u>	<u>242,053</u>	<u>202,509</u>
<b>Current liabilities</b>					
Trade accounts payable	12	10,942	7,002	10,942	7,002
Payables with respect to open derivative positions	6	329,499	-	-	-
Liabilities with respect to securities that were not transferred to the Stock Exchange Clearing House on a timely basis	7	143,001	-	-	-
Payables and other current liabilities	13	26,425	27,592	22,702	23,353
Capital notes	15	-	2,600	-	2,600
		<u>509,867</u>	<u>37,194</u>	<u>33,644</u>	<u>32,955</u>
<b>Long-term liabilities</b>					
Accrued severance pay, net	14	<u>5,167</u>	<u>3,897</u>	<u>5,167</u>	<u>3,897</u>
<b>Contingent liabilities and special commitments</b>	16				
<b>Shareholders' equity</b>		<u>203,242</u>	<u>165,657</u>	<u>203,242</u>	<u>165,657</u>
		<u>718,276</u>	<u>206,748</u>	<u>242,053</u>	<u>202,509</u>

(\*) In the matter of initial implementation accounting standard No. 22 commencing January 1, 2006 and its effect on the balance sheets – see Notes 6 and 7.

Saul Bronfeld  
Chairman of the Board

Ester Lebanon  
CEO and Director

Joseph Treister  
Senior Vice President  
Administration and Finance

Tel Aviv, April 25, 2007

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

**THE TEL-AVIV STOCK EXCHANGE LTD**  
Approval date of the financial statements  
**CONSOLIDATED STATEMENTS OF OPERATIONS**  
(NIS in thousands)

		Year ended December 31		
		2 0 0 6	2 0 0 5	2 0 0 4
	<u>Note</u>			
Revenues from services				
Trading and clearing commissions		112,553	114,723	95,340
Securities registration and annual fees		34,896	28,575	20,726
Clearing House services for the TASE members and for public companies		15,228	12,788	10,150
Presentation of trade as well as other data		24,762	20,442	16,980
Other		3,143	1,741	967
		<u>190,582</u>	<u>178,269</u>	<u>144,163</u>
Cost of revenues				
Salaries and social benefits	17	81,666	71,984	66,807
IT and communication expenses		15,528	11,705	11,794
Rent, municipal taxes and building maintenance		9,462	9,121	8,015
General and administrative expenses		13,678	10,765	8,963
Fee to Israeli Securities Authority		7,078	7,306	7,243
Depreciation		11,026	10,267	8,870
Premiums in respect of the Ma'of Risk Fund		8,085	8,725	7,706
		<u>146,523</u>	<u>129,873</u>	<u>119,398</u>
Operating income before net financing		44,059	48,396	24,765
Financing income, net	19	<u>11,360</u>	<u>12,618</u>	<u>7,864</u>
Operating income after net financing		55,419	61,014	32,629
Other income(expenses), net		<u>(53)</u>	<u>87</u>	<u>114</u>
Pre-tax income		55,366	61,101	32,743
Income taxes	20	<u>18,011</u>	<u>20,522</u>	<u>12,090</u>
Income after income taxes		37,355	40,579	20,653
Company's share in earnings of investees, net		<u>230</u>	<u>246</u>	<u>225</u>
Net income for the year		<u>37,585</u>	<u>40,825</u>	<u>20,878</u>

**THE TEL-AVIV STOCK EXCHANGE LTD**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(NIS in thousands)

	Year ended December 31,		
	2006	2005	2004
<b>CASH FLOWS - OPERATING ACTIVITIES</b>			
Net income for the year	37,585	40,825	20,878
Adjustments required to present cash flows provided by operating activities (Appendix A)	7,328	7,979	10,993
Net cash provided by operating activities	44,913	48,804	31,871
<b>CASH FLOWS - INVESTING ACTIVITIES</b>			
Additions to fixed assets	(18,684)	(15,410)	(9,008)
Proceeds from disposition of fixed assets	193	204	246
Purchase of marketable securities	(123,291)	(127,079)	(106,842)
Proceeds from the disposition of marketable securities	108,408	94,009	77,589
Dividends received from an affiliate	278	257	308
Purchase of an initially consolidated subsidiary (Appendix B)	(336)	-	-
Net cash used in investing activities	(33,432)	(48,019)	(37,707)
<b>Cash Flows - Financing Activities</b>			
Capital note repayment	(2,600)	-	-
Net cash used in financing activities	(2,600)	-	-
Increase (decrease) in cash and cash equivalents	8,881	785	(5,836)
Cash and cash equivalents at beginning of year	17,264	16,479	22,315
Cash and cash equivalents at end of year	26,145	17,264	16,479